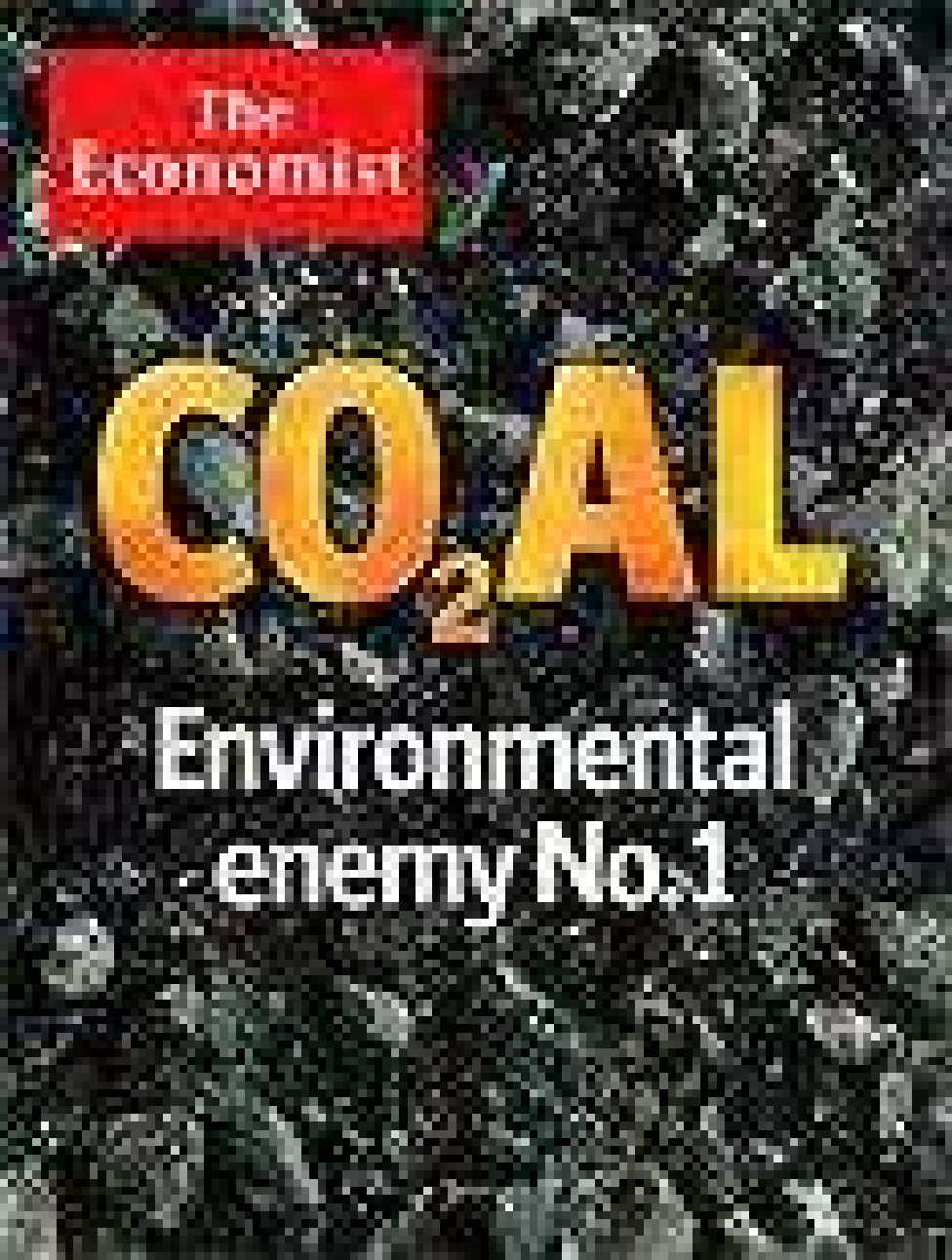
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POLITICS THIS WEEK

BUSINESS THIS WEEK

OPINION
Leaders
Letters

WORLD
United States
The Americas
Asia
Middle East & Africa
Europe
Britain
Country Briefings
Cities Guide

SURVEYS

BUSINESS
Management Reading
Business Education
Executive Dialogue

FINANCE & ECONOMICS
Economics Focus
Economics A-Z

SCIENCE & TECHNOLOGY
Technology Quarterly

PEOPLE
Obituary

BOOKS & ARTS
Style Guide

MARKETS & DATA
Weekly Indicators
Currencies
Big Mac Index

DIVERSIONS

RESEARCH TOOLS

CLASSIFIEDS

DELIVERY OPTIONS
E-mail Newsletters
Mobile Edition
RSS Feeds

ONLINE FEATURES
Cities Guide Go
Country Briefings Go
Audio interviews Go
Classifieds Go

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## Print Edition July 6th 2002

**Environmental enemy No. 1**
Cleaning up the burning of coal would be the best way to make growth greener ... More on this week's lead article

### The world this week

Politics this week
Business this week

### Leaders

The environment
**Environmental enemy No. 1**

ID cards in Britain
**Identity crisis**

Vivendi
**A French exception**

The International Criminal Court
**Not (quite) strangled at birth**

Asia's economies
**Five years on**

### Letters

**On America, Israel and Palestine**

### Special Report

Arab development
**Self-doomed to failure**

Jordan's democratic freeze
**The king knows best**

### United States

Corporate scandals and politics
**The backlash against business**

The retirement of J.C. Watts
**Ave atque vale**

The International Criminal Court
**Right to the brink**

Troubled youth
**Band on the run**

Recycling
**Waste of time**

Training doctors
**Too little money, too much paper**

Lexington
**Inching towards reform**

### The Americas

Bolivia's election
**Desperate for change—and for more of the same**

Montesinos on trial
**One down, just 70 or so to go**

Argentina
**Duhalde heads for the door**

Cuba's economy
**The disaster is now "irrevocable"**

**Brazil's football scandals forgotten**

### Asia

India
**The irresistible rise of L.K. Advani**

Pakistan
**Constitutional quagmire**

Afghanistan
**Taking lives, losing friends**

North Korea, South Korea and America
**The dead are not the only casualties**

China's Three Gorges' project
**Dam shame**

### Middle East & Africa

**Previous print editions**
Jun 29th 2002
Jun 22nd 2002
Jun 15th 2002
Jun 8th 2002
Jun 1st 2002
**More print editions and covers »**

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### A survey of the global environment

**The great race**
**Flying blind**
**Blowing hot and cold**
**Local difficulties**
**Working miracles**
**The invisible green hand**
**Insuring a brighter future**
**Sources and acknowledgments**
**Offer to readers**

### Business

Chief financial officers
**Too creative by 50%?**

Vivendi Universal
**Maître dethroned**

Weblogging
**The trees fight back**

Xerox
**Corruption without contrition**

Containers
**Ports in a storm**

America's defence industry
**On manoeuvres**

Weil, Gotshal & Manges
**Mopping up**

Face value
**Called to account**

### Special Report

East Asian economies
**The lost (half) decade**

### Finance & Economics

Accounting scandals and the SEC
**Harvey Pitt fights back**

Credit markets
**On to the pyre**

American banks
**A murky sort of pond life**

Japanese banks
**Nationalised once, nationalised again?**

Borsa Italiana
**Carina**

Italian bonds
**Relations unsettled**

Insurance broking
**Jackpot**

Economics focus
**The Fund bites back**

### Science & Technology

Carbon sequestration
**Fired up with ideas**

Embryology

A report from Congo
**Africa's great war**

## Europe

Turkey's government
**No place for a worn-out prime minister**

Italy's government
**A blow to the prime minister**

Portugal's public finances
**Too much red ink for the euro-zone**

Denmark and asylum
**The welcome-mat has gone**

France's new plan
**Too good to be true?**

A controversial German appointment
**Unwed mother as family guardian**

Charlemagne
**Farmer Franz Fischler**

## Britain

Britain and America
**Listen, George**

Politics and television
**Unreality TV**

Currencies and xenophobia
**Many a true word...**

Hotel prices
**Chequing in**

Housing in the south-east
**Gordon versus the nimbies**

Railways
**Puff, puff**

Digital television
**The odd couple**

Bagehot
**Happy birthday, BT**

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**Left, right or wrong**

Hand-washing
**How to save 1m children a year**

## Books & Arts

Treating a stroke
**It takes more than prayers**

Mars
**A rose-red, dried-up world**

Lucian Freud
**Bare flesh, hidden soul**

**The troubles in Ireland**

The history of socialism
**Some uncommon common people**

New American fiction
**To hell and back**

Bestsellers in Australia and Canada
**What the world is reading**

## Obituary

**Pierre Werner**

## Economic and Financial Indicators

**Overview**

**Output, demand and jobs**

**Prices and wages**

**Economic forecasts**

**Money and interest rates**

**The Economist commodity price index**

**Stockmarkets**

**Trade, exchange rates and budgets**

**Global mergers and acquisitions**

## Emerging-Market Indicators

**Overview**

**Cost-of-living index**

**Economy**

**Financial markets**

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|---|---|---|---|---|---|
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# Politics this week

Jul 4th 2002
From The Economist print edition

## Hamas bomb-maker killed

Reuters

Israeli soldiers killed Muhanad al-Taher, a **Hamas bomb-maker** Israel held responsible for 117 deaths. An Israeli newspaper said Israel's army had run out of targets on its “most wanted” list.

**Yasser Arafat** sacked two powerful security chiefs. At first they seemed unwilling to go, initiating a power struggle. However, one later resigned, saying he would stand in an election for the Palestinian presidency next January.

Tension between **India and Pakistan** rose after India claimed that militant groups were again crossing into its part of Kashmir. Pakistan denied the accusation; its promise to end incursions was part of a deal to stop the nuclear-armed neighbours from going to war.

The UN predicted that **AIDS** will kill 70m people in the next 20 years, mostly in poor countries, unless more is done to fight the disease. About 40m people are now infected with HIV, the virus that causes AIDS, and 20m have died of it since it was discovered in 1981.

## Rough justice

America threatened to veto a routine extension of the UN mission in Bosnia, for fear that its soldiers might be prosecuted by the **International Criminal Court**, which came into being on July 1st. The UN Security Council is working on a compromise.

See article: Court quarrel continues

Mohammed Saffi, a stepson of Saddam Hussein, was arrested in Miami, having entered the United States to attend a **flight-training** seminar without the right visa.

In a five-to-four decision, the Supreme Court upheld the constitutionality of **school vouchers** in Cleveland, Ohio. Opponents say the programme flouts the separation of church and state, because so many voucher children go to religious schools. The court decided that parents could choose where the money was spent—not the state.

See article: Inching towards reform

A Bureau of Indian Affairs employee was charged with starting one of two **forest fires** that merged to become the largest in Arizona's history. More than 4,000 fire-fighters were deployed to fight the “Rodeo” blaze which spread over 452,000 acres and destroyed more than 400 homes.

EPA

Steve Fossett, a millionaire adventurer, succeeded in his sixth attempt to become the first person to fly, solo, a **balloon** around the world, when he crossed the west Australian coastline less than a fortnight after he took off in *Spirit of Freedom*.

## Pain control

**Italy's** big-mouthed interior minister, Claudio Scajola, opened it once too often: he had to resign, after reportedly calling a murdered governmental labour adviser “a pain in the arse”.

See article: A blow to Italy's prime minister

After weeks of three-party haggling, a deal brought **the Netherlands** to the brink of a centre-right coalition government, led by the Christian Democrats' Jan Peter Balkenende. The populist party of the late Pim Fortuyn, number two in the new parliament, is promised four cabinet seats but little policy satisfaction.

A Spanish judge told Batasuna, the political arm of the Basque separatist **terror group** ETA, to pay a fine of *euro*24m ($23.6m) for being responsible for harming people and property. Batasuna's leader said that the ruling amounted to a ban.

In a message to parliament, President Jacques Chirac promised to “resume the long march, so often thwarted, toward decentralisation” for **France**.

See article: France's president unveils his plan for the future

The European Parliament voted that foods and animal feeds containing more than 0.5% **genetically modified** ingredients should be labelled as such. The decision is a blow to biotech supporters who wanted a higher threshold.

Two jets collided over southern Germany, killing more than 70 people. One was flying from Moscow to Barcelona, carrying mainly children from the Russian republic of **Bashkortostan**; the other was a cargo plane heading from Bahrain to Belgium. Swiss air-traffic controllers came under suspicion.

## Divide and rule

France joined America in recognising Marc Ravalomanana as president of **Madagascar**. Mr Ravalomanana looked set to win control of the whole island nation, as his soldiers advanced on the northern stronghold of his rival, Didier Ratsiraka, who disputes Mr Ravalomanana's claim to have won an election in December.

In **Côte d'Ivoire**, the opposition leader Alassane Ouattara won back his citizenship, which had been revoked, apparently to prevent him running for president.

A case brought by Khaled Nezzar, a former Algerian defence minister, against Habib Souaidia, an ex-army officer and the author of “The Dirty War 1992-2000”, began in a Paris court. Mr Souaidia alleges that soldiers in **Algeria's civil war** disguised themselves as rebels and massacred civilians.

## Warshipping news

AP

Warships from **North and South Korea** fired on each other in disputed waters in the worst clash between the two countries for three years. A South Korean ship sank and four sailors died. The South suspended rice shipments to the famine-stricken North.

See article: The Koreas and America

Some 40 civilians were said to have died when American aircraft mistakenly attacked a wedding party in southern **Afghanistan**.

See article: Accidental killings in Afghanistan

Two Chinese diplomats were shot dead in Bishkek, the capital of **Kirgizstan**. Police blamed Uighurs fighting for a separate state in China.

## Order of the boot

Brazil beat Germany 2-0 to win football's **World Cup** for an unprecedented fifth time. Both goals were by Ronaldo, making a total of eight in this year's tournament, a feat unequalled by any player since Brazil's Pele in 1970.

See article: Heroes' return

**Argentina's** President Eduardo Duhalde, facing public angerat his failure to solve the country's economic crisis, said he would bring forward its elections by six months, to next March.

See article: Argentina and Brazil

After the first round of **Bolivia's elections**, Gonzalo Sanchez de Lozada, a free-market ex-president, looked set to make a comeback. Evo Morales, the coca growers' leader, surged to third place after America's ambassador urged voters to reject him.

See article: Bolivia's election

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# Business this week

Jul 4th 2002
From The Economist print edition

## Maître dethroned

Jean-Marie Messier stepped down as chairman and chief executive of **Vivendi Universal**, the French media giant. But the move was not enough to satisfy shareholders, who continued to sell because of doubts about the company's finances. Vivendi's troubles may not dent Mr Messier's bank account, however, as he was reported to be negotiating a *euro*20m ($19.5m) severance package. He will be replaced by Jean-René Fourtou, vice-chairman of Aventis, a multinational drug company.

See article: The French fix

**WorldCom** disclosed that it had expanded its accounting probe beyond the $3.8 billion in overstated profits that it revealed last week. John Sidgmore, chief executive, said that WorldCom could avoid bankruptcy, but conceded that lenders would be better off if the firm filed for Chapter 11 protection.

See article: Chief financial officers

Shares in **France Telecom** rose by a quarter after an official from the French finance ministry said that the government was contemplating a renationalisation of the company. Another official later denied this. Some speculated that the contradictory comments were a ploy to squeeze short-sellers.

**Northrop Grumman** strengthened its claim to be in the top rank of defence contractors when it bought **TRW**, a car-parts and defence group, for $7.8 billion. It beat General Dynamics and BAE Systems. BAE will now have to rethink its strategy in America.

## Bank drama

Lukas Mühlemann, **Credit Suisse's** chairman and chief executive, will step down as chairman at its annual shareholders' meeting in 2003, but stay on as chief executive. Markets were rife with rumours of possible bids for Credit Suisse, taking advantage of the depressed share price of Switzerland's second-largest bank. Mr Mühlemann may yet find himself ousted from the bank altogether.

Anxiety over Vivendi and WorldCom caused **stockmarkets** to plunge. America's S&P 500 hit a four-and-a-half-year low; London's FTSE 100 hit a five-year low. The **dollar** sank nearly to parity with the euro before bouncing back, buoyed by reports that America's economic expansion is stronger than Europe's.

Two of Britain's largest **initial public offerings** were called off because of unfavourable market sentiment. Yell, the country's biggest phone directory, and Focus Wickes, its second-largest DIY retailer, will try again if markets rebound.

**Merrill Lynch**, America's biggest stockbroking firm, may cut jobs in Europe by as much as 20%. It blames poor market conditions—specifically, the dearth of mergers and initial public offerings.

Hefty losses since the September 11th attacks may cause the number of syndicates at **Lloyd's of London** to fall by nearly half, according to Swiss Re, one of the world's largest reinsurers. London insurers are facing growing competition from new markets in such places as Bermuda.

Another case of corporate mischief came to light when a Spanish investigating judge found evidence that the chairman of **Banco Santander Central Hispano**, Emilio Botin, and four executives were responsible for selling financial products that helped clients to avoid paying taxes. If they are found guilty, the

executives could be jailed.

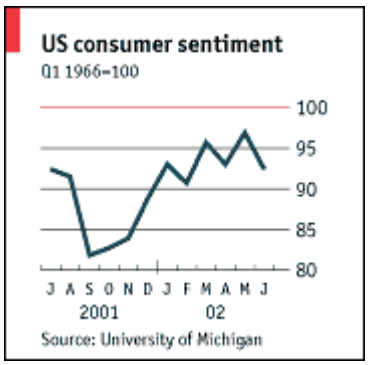
**Euroclear**, an international settlement agency, will take over **Crest**, a British peer, to create Europe's largest settlement system for stocks and bonds. The new, larger Euroclear will account for over half of European shares.

## Drugged out

**Schering-Plough** and **Upsher-Smith Laboratories** breathed a sigh of relief after a court rejected Federal Trade Commission charges that the two broke antitrust law by keeping less expensive versions of a heart medicine off the market. The judge ruled that a 1997 patent deal between the two "complied with the law in all respects."

Shares in **Elan**, an Irish drug maker, tumbled by 56% in one day, after the company announced that a decline in the value of its investments and its business recovery plan would cause "significant" charges. Elan is no stranger to falling prices: shareholders' worries over the quality of its accounts had already pushed its shares down heavily earlier this year.

The University of Michigan's **consumer-sentiment** index fell by 4.5 points to 92.4, the largest percentage point drop since September 11th. Consumer spending accounts for around two-thirds of America's output. The fall suggests that the American economic recovery could be weaker than many had expected. The euro area's indices of consumer and business confidence also fell.

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The environment

# Environmental enemy No. 1

Jul 4th 2002
From The Economist print edition

**Cleaning up the burning of coal would be the best way to make growth greener**

IS GROWTH bad for the environment? It is certainly fashionable in some quarters to argue that trade and capitalism are choking the planet to death. Yet it is also nonsense. As our survey of the environment this week explains, there is little evidence to back up such alarmism. On the contrary, there is reason to believe not only that growth can be compatible with greenery, but that it often bolsters it.

This is not, however, to say that there are no environmental problems to worry about. In particular, the needlessly dirty, unhealthy and inefficient way in which we use energy is the biggest source of environmental fouling. That is why it makes sense to start a slow shift away from today's filthy use of fossil fuels towards a cleaner, low-carbon future.

There are three reasons for calling for such an energy revolution. First, a switch to cleaner energy would make tackling other green concerns a lot easier. That is because dealing with many of these—treating chemical waste, recycling aluminium or incinerating municipal rubbish, for instance—is in itself an energy-intensive task. The second reason is climate change. The most sensible way for governments to tackle this genuine (but long-term) problem is to send a powerful signal that the world must move towards a low-carbon future. That will spur all sorts of innovations in clean energy.

The third reason is the most pressing of all: human health. In poor countries, where inefficient power stations, sooty coal boilers and bad ventilation are the norm, air pollution is one of the leading preventable causes of death. It affects some of the rich world too. From Athens to Beijing, the impact of fine particles released by the combustion of fossil fuels, and especially coal, is among today's biggest public-health concerns.

## Dethroning King Coal

The dream of cleaner energy will never be realised as long as the balance is tilted toward dirty technologies. For a start, governments must scrap perverse subsidies that actually encourage the consumption of fossil fuels. Some of these, such as cash given by Spain and Germany to the coal industry, are blatantly wrong-headed. Others are less obvious, but no less damaging. A clause in America's Clean Air Act exempts old coal plants from complying with current emissions rules, so much of America's electricity is now produced by coal plants that are over 30 years old. Rather than closing this loophole, the Bush administration has announced measures that will give those dirty old clunkers a new lease on life. Nor are poor countries blameless: many subsidise electricity heavily in the name of helping poor people, but rich farmers and urban elites then get to guzzle cheap (mostly coal-fired) power.

That points to a second prescription: the rich world could usefully help poorer countries to switch to cleaner energy. A forthcoming study by the International Energy Agency estimates that there are 1.6 billion people in the world who are unable to use modern energy. They often walk many miles to fetch wood, or collect cow dung, to use as fuel. As the poor world grows richer in coming decades, and builds thousands of power plants, many more such unfortunates will get electricity. That good news will come with a snag. Unless the rich world

**The harm done to human health and the environment from burning fossil fuels is not**

intervenes, many of these plants will burn coal in a dirty way. The resultant surge in carbon emissions will cast a grim shadow over the coming decades. Ending subsidies for exporters of fossil-fuel power plants might help. But stronger action is probably needed, meaning that the rich world must be ready to pay for the poor to switch to low-carbon energy. This should not be regarded as mere charity, but rather as a form of insurance against global warming.

**reflected in the price of those fuels, especially coal, in most countries**

The final and most crucial step is to start pricing energy properly. At the moment, the harm done to human health and the environment from burning fossil fuels is not reflected in the price of those fuels, especially coal, in most countries. There is no perfect way to do this, but one good idea is for governments to impose a tax based on carbon emissions. Such a tax could be introduced gradually, with the revenues raised returned as reductions in, say, labour taxes. That would make absolutely clear that the time has come to stop burning dirty fuels such as coal, using today's technologies.

## The dawning of the age of hydrogen

None of these changes need kill off coal altogether. Rather, they would provide a much-needed boost to the development of low-carbon technologies. Naturally, renewables such as solar and wind will get a boost. But so too would “sequestration”, an innovative way of using fossil fuels without releasing carbon into the air (see article).

This matters for two reasons. For a start, there is so much cheap coal, distributed all over the world, that poor countries are bound to burn it. The second reason is that sequestration offers a fine stepping-stone to squeaky clean hydrogen energy. Once the energy trapped in coal is unleashed and its carbon sequestered, energy-laden hydrogen can be used directly in fuel cells. These nifty inventions can power a laptop, car or home without any harmful emissions at all.

It will take time to get to this hydrogen age, but there are promising harbingers. Within a few years, nearly every big car maker plans to have fuel-cell cars on the road. Power plants using this technology are already trickling on to the market. Most big oil companies have active hydrogen and carbon-sequestration efforts under way. Even some green groups opposed to all things fossil say they are willing to accept sequestration as a bridge to a renewables-based hydrogen future.

Best of all, this approach offers even defenders of coal a realistic long-term plan for tackling climate change. Since he rejected the UN's Kyoto treaty on climate change, George Bush has been portrayed as a stooge for the energy industry. This week, California's legislature forged ahead by passing restrictions on emissions of greenhouse gases; a Senate committee has acted similarly. Mr Bush, who has made surprisingly positive comments about carbon sequestration and fuel cells, could silence the critics by following suit. By cracking down on carbon and embracing hydrogen, he could even lead.

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ID cards in Britain

# Identity crisis

Jul 4th 2002
From The Economist print edition

**Behind government plans to introduce identity cards lies a broader and more worrying issue**

POLICIES, says Peter Lilley, a former Tory minister, are rather like houses. If one of them has been on the market for a long time, it's probably because there is something wrong with its foundations.

That is one of the reasons why the government's consultation paper on identity cards, published on July 3rd, was received with some suspicion. Identity cards were in use during the second world war, and successive governments have explored, and rejected, the idea of reintroducing them. The pattern has become familiar. Civil servants persuade the politicians that it would be useful to be able to keep more tabs on the public, the public objects to the idea, and the politicians give it up as being more trouble than it is worth.

That may well happen this time around, too. The government's nervousness about the issue is clear from its approach. Instead of calling these bits of plastic ID cards, it is calling them “entitlement cards”. Instead of spelling out proposals, it has published a “consultation paper” which it says it hopes will get a debate going. It wants, in other words, to find out how cross the idea makes people. And the signs are that the idea makes quite a lot of people quite cross.

But the fuss about ID cards is misdirected. The ID cards proposal is a small, visible manifestation of a huge, invisible process of the collection, computerisation and centralisation of personal information that is going on. Much larger questions—such as whether the computers at the Inland Revenue that know everything about people's tax position should be allowed to talk to the computers at the Department of Work and Pensions that know everything about people's benefit claims—are being decided with no public debate at all. The process of acquiring new information about people and using it in new ways will go on whether or not the government opts for ID cards, and will continue to transform the machinery of government, and the state's relationship with its citizens.

## Efficiency can be dangerous

The reason the government is computerising all this information is not because it is bent on attacking personal freedoms, but because it wants to make its systems work more efficiently. This is something every taxpayer also wants. Investing in IT is crucial to improving public services while keeping costs down.

Yet there is a trade-off between efficiency and liberty. An inefficient state can never repress its people as effectively as an efficient one. What, then, is the citizen supposed to hope for? A government with effective, and therefore potentially dangerous, machinery, or a government that doesn't work very well?

The only way of reconciling efficiency with liberty is to balance the government's new powers with new rights. Let the databases grow. Let the computers talk to each other. Let the ID cards be issued. But give citizens the right to see any information the state holds about them.

For countries with a tradition of freedom of information, the idea that citizens should have access to their files is uncontentious. Not so in Britain, where the government has a tradition of withholding information from its citizens. Yet if people knew what the government knew, they would worry less; and if they

worried less, they would be more inclined to give the government the benefit of the doubt over small issues like ID cards.

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**Vivendi**

# A French exception

Jul 4th 2002
From The Economist print edition

**Like corporate France as a whole, the media giant is exceptional, but only up to a point**

AP

JEAN-MARIE MESSIER was meant to be an emblem of French corporate success, and of its ability to break out of a cosy French business culture and straddle the transatlantic divide. But in the end, the man who turned a French water utility into a global media giant, Vivendi Universal, was too French for the Americans and too American for the French. His eviction this week followed a revolt on behalf of disgruntled shareholders. But the worry is that it may also reflect French business's atavistic desire to retreat to its traditional clubbish ways—and the politicians' encouragement of this.

On the face of it, Mr Messier's removal seems to be the responsible reaction of board members to the company's ailing share price and confused strategic direction. Mr Messier, who set out to create a dazzling multimedia business, overpromised and overpaid. In his rush to build his empire, he failed either to make the bits stick together properly, or to convince investors that they made sense—all the while piling up increasingly unmanageable debts (see article). Since he had the job of both chairman and chief executive, and thrived as the company's public face—*Fortune* magazine called him “the country's first rock-star CEO”, while *Paris-Match* featured him ice-skating in Central Park and flying in the corporate jet—he was also the natural fall guy.

Yet there is more to his departure than meets the eye. What tipped the balance in favour of his expulsion was the decision by the French board members, who form the majority, to desert him and back their North American colleagues. This, in turn, seems to have been guided by members of the French elite, notably Claude Bébéar, chairman of the insurance giant AXA, and by elements in President Jacques Chirac's governing conservative party. Who manoeuvred whom may never be known, but the overriding concern was plain: Vivendi had to be run by a “proper” Frenchman, and its treasured assets had to be kept in French hands.

The reason for a sense of dismay at all this is twofold. First, it comes at a time of resurgent nationalistic feeling in France, one that politicians have been finely attuned to ever since the far-right Jean-Marie Le Pen did so shockingly well earlier this year. It can be detected in Mr Chirac's stubborn support of Electricité de France, the state-owned utility that has expanded merrily abroad while resisting liberalisation of the domestic energy market. It will be seen again when France defends farm subsidies against European plans to liberalise them. It can even be heard in the vague mutterings of the new centre-right government about a possible renationalisation of France Telecom. The common theme is “France first”—a sentiment that the recent loss of confidence in corporate America and Anglo-Saxon capitalism is fuelling.

If this attitude limits the list of buyers for politically sensitive Vivendi businesses—notably telecoms, utilities and Canal Plus, the pay-TV operation—to French companies, it will clearly not serve shareholders' best interests. But more broadly, the more corporate France falters, the greater the temptation will be for the French government to step in to defend national champions. Other European governments, many of which share to varying degrees France's suspicions of the American corporate model, may well follow suit.

The second reason for disappointment is that corporate France is no longer the inward-looking cultural exception it once was. Far more young French executives study and work abroad now, and a growing number of French companies have overseas interests, foreign board members and investors. Such

changes have taken place only up to a point: the corporate elite remains close-knit, suspicious of outsiders and still tends to recruit from a narrow pool of technocratic managers. But the risk is that the Vivendi affair may herald an even more retrograde step back to the bad old ways.

## Hollywood ending

In the end, Mr Messier may have embodied Vivendi in more ways than he meant to. The man who dared to declare that “the French cultural exception is dead” was back on more traditional territory this week. In an interview, Mr Messier defended his record in patriotic terms. “That a French company has become the world leader in music, the world leader in cinema, is an extraordinary achievement”, he said, adding that he had agreed to resign only on condition that his successor was French. If Mr Messier was seduced by America, and America seduced by how he had fallen for it, their mutual love has turned out to be as deep as an average Hollywood movie.

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The International Criminal Court

# Not (quite) strangled at birth

Jul 4th 2002
From The Economist print edition

**America has little to fear, and the world a good deal to gain, from the new criminal court**

Get article background

Reuters

THERE have been plenty of stand-offs within the United Nations' Security Council over the years, but few as dispiriting as the one that threatened this week to undermine the peacekeeping effort in Bosnia. On one side stood the United States, promising to sustain its veto of a routine extension of the UN mandate in Bosnia unless the council agreed to grant UN peacekeepers immunity from the newly created International Criminal Court (ICC). On the other side stood all 14 other council members, led by Britain and France, insisting that a formal grant of immunity was not just unnecessary, but might strangle the court at its birth. Have America's relations with Europe grown so ill-tempered that they cannot even resolve a dispute which looks to most people like a legal technicality?

The depressing answer seems to be yes. Although the dispute was suspended at the last minute by an agreement to extend the UN mandate by a further 12 days, the two sides should have been able to sort out their differences more quickly. Yet, as if to confirm the accusations of unilateralism directed against it, the Bush administration has not been much interested in compromise. It has hardened America's long-standing opposition to the court into outright hostility.

**Have America's relations with Europe grown so ill-tempered that they cannot even resolve a dispute which looks to most people like a legal technicality?**

American officials have directed a barrage of criticism at the court, most of it ill-founded or simply wrong (see article), even though nearly all of America's objections have already been dealt with. After all, fears of a rogue court were shared by America's allies—especially by Britain and France, who also send their soldiers abroad as peacekeepers. Second, in an effort to assuage American concerns, its allies have encouraged American officials to help shape the rules that will govern the court's operations, despite the fact that there was little prospect of America ratifying the treaty.

The Security Council dispute is largely symbolic, but no less important for that. From the start, the prospects that Americans working under a UN mandate would end up before the ICC were almost nil. UN soldiers and officials already enjoy immunity from local prosecution. If they commit crimes, they are supposed to be repatriated and tried by their own countries. They would have been subject to the ICC's jurisdiction only if they had committed widespread and systematic war crimes or crimes against civilians (random shootings or mistakes such as this week's bombing of an Afghan wedding are too ordinary for the ICC). Even in the unlikely event that American generals intentionally ordered widespread atrocities, the ICC could not act unless America itself refused to investigate or prosecute them, or staged a sham trial to exonerate them. It seems unlikely that either condition could be met in a transparent democracy such as the United States without sparking a huge public outcry. Nevertheless, what the American government is at pains to establish is that there are no circumstances, no matter how grievous, in which any American anywhere would be subject to ICC jurisdiction. To get its way, it has threatened to shut down all UN peacekeeping.

## At least give the thing a chance

If the prospect of an ICC prosecution against American soldiers or officials is so remote, why haven't

Britain and France backed down? They still might. But they were right to dig their heels in because conceding all of America's demands would have been tantamount to letting it, through a threatened veto in the council, rewrite a treaty already ratified by 76 countries. Any future compromise must avoid that, and must stop short of incorporating into law permanent blanket immunities for anyone. The court's supporters rightly believe that these might irreparably damage the ICC's claim to dispense even-handed justice.

America should now drop its hostility to the court. There are already more than enough protections for Americans against politicised prosecutions. The court is supported not just by Europeans but also many poorer nations where atrocities are a real danger. It deserves a chance to prove itself. If it succeeds, it could yet become an important tool in bringing mass murderers to justice and extending the rule of law—goals which, as George Bush has often said, are not only in the world's interest, but America's as well.

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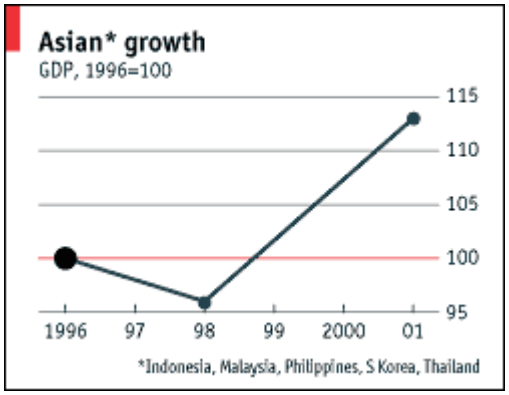
Asia's economies

# Five years on

Jul 4th 2002
From The Economist print edition

**What has been learned since Asia's high-flying economies fell to earth?**




THAILAND'S forced devaluation of the baht, five years ago this week, marked the beginning of a regional economic crisis that threatened at one stage to engulf the world. The emergency seemed to come from nowhere, and to dash the prospects of countries that had been seen as the most successful in the developing world. What happened over the following year undermined confidence not only in the emerging markets and in institutions such as the International Monetary Fund and the World Bank, but also in the consensus that had seemed to be taking shape about how best to achieve economic development.

Five years on, how does East Asia look? In a word, good. Just as the region had been applauded too euphorically in the years leading up to the crisis, so the mood of despondency was overdone in the immediate aftermath.

In much of East Asia, recovery began soon after the crisis first struck. In Thailand, GDP fell by more than 10% in 1998—but then grew by 4% the next year. In South Korea, output fell by 7% in the first year; over the next 12 months, it rose by 11%. In most of the region, as a result, the recovery is at least three years old. In South Korea, output last year was almost a quarter higher than before the collapse began, and foreign direct investment (much safer than short-term debt, its pre-crisis staple) is flowing in more freely than ever. So one lesson to draw from the history of the past decade is: don't get carried away. Economic miracles are rarely all they seem; luckily, the same goes for economic cataclysms.

Another lesson concerns exchange rates. The calamity in East Asia underlined the hazards of “fixed” exchange rates, especially when combined with hasty capital-account liberalisation and poor regulation of domestic finance. For a while, the collapse of the region's currency pegs gave rise to a new conventional wisdom. Let currencies float, or fix them irrevocably—there is no middle way. Today, the options seem narrower still: Argentina is in trouble partly because it staked everything on trying to fix its peso permanently against the dollar. Yet the move to floating creates difficulties of its own, especially when it comes to controlling inflation. It should make crashes less likely, and less violent when the worst happens—but crises will keep coming, floating or no.

**The move to floating exchange rates should make crashes less likely, and less violent when the worst happens—but crises will keep coming**

These are timid generalisations, but it would be rash to infer much more: East Asia's economies, on closer examination, are a mixed bunch. Each has its own political and/or economic challenges to face (see article). A future risk, in fact, is that other economies may try to follow the example of South Korea, the best post-crisis performer, too slavishly or uncritically, applying methods that worked in its case to their own different circumstances.

South Korea's recovery has been based partly on a recovery of exports (notably exports to other Asian countries), but more strikingly on surging domestic demand. That is something Thailand, the Philippines and others may be seeking to emulate, using budget policy to stimulate consumption. They need to remember that the fiscal tool must be used with care, if public debt is not to rise out of control. Most of all, they should note that South Korea's recovery, albeit led by domestic demand, was based on a thorough reform and restructuring of the domestic banking system. Other governments in the region have flinched from that task.

## Stop drawing, start building

The Asian crisis also gave rise to a heated debate about the response of rich-country governments and the international financial institutions, especially the IMF. There was a flurry of interest in reforms to the "international financial architecture", but disappointingly little has happened as a result. Some of the mooted reforms—such as creating an international equivalent of domestic bankruptcy—are so ambitious and so complicated that, whatever their merits, they could not be done quickly. Other ideas, such as including collective-action clauses in bond contracts (thereby facilitating debt restructuring, should the need arise), could perfectly well have been acted upon already. They have not been.

The row over the IMF shows little sign of abating (see article). But all in all, the recovery in the region speaks well of the way the crisis was managed. Mistakes were made, no doubt. The Fund itself acknowledges as much—and, to its credit, showed a willingness to correct its errors promptly. To have done better at the time, without benefit of hindsight, would have been a tall order. So it will prove in the next emergency.

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# Letters

Jul 4th 2002
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
FAX: 020 7839 2968 E-MAIL: letters@economist.com

## Israel and Palestine

SIR – Your editorial considers George Bush's speech on the Middle East a "one-sided peace vision" and suggests that it was driven by domestic American politics ("George Bush's plan for peace", June 29th). You say that America and Europe "do not agree on who the bad guys are. And this makes all the difference."

Amazing. After the gallons of innocent Israeli blood spilled, and the tons of Palestinian explosives, nails and rat poison devoted to terrorism, *The Economist*, the governments of Europe and the Arab world cannot decide who the bad guys are.

You expressed disappointment that Mr Bush's speech did not call on Israel to return to 1967 borders (perhaps because UN Resolution 242 doesn't call for it) nor condemn the "illegal" Israeli settlements (perhaps because official United States legal advisers determined that they were not).

*The Economist* should attempt to be more balanced in its evaluations.

Arthur Gober
Long Beach, New York

**Editor's note:** Though presented as if it were an individual letter to the editor, scores of letters using almost identical language were sent to *The Economist* this week in an orchestrated campaign.

SIR –"It is not all as bad as it sounds. Mr Bush has told Israel that the Palestinians need a state, and the Palestinians that they cannot win one through terrorism."

You imply that the problem boils down to a simple, one-for-each acceptance package: the Israelis must recognise the rights of the Palestinians to a homeland, and the Palestinians must accept this homeland cannot be achieved through terrorism. However, the crux of the problem is that, while the Israelis have long recognised the Palestinian right to a state, the Palestinians have not realised that terrorism will not pay.

Tulli Padwa
Antwerp

SIR – In a June 27th e-mail an American organisation, referring to your reporting of George Bush's Middle East speech, said "[it] even suggested that Bush was motivated by domestic American politics." Now that really is taking chutzpah to a new high—or should I say low?

Marshall Foreman
Florida

SIR – You claim that violence has brought the whole Palestinian nation into disrepute ("An opportunity missed", June 15th), the implicit criticism being that suicide bombings are immoral. Our own record in the West should make us less hasty in our condemnation. One of the aims of aerial bombing in the second world war was to terrorise the civilian population into surrender. Allied aircrew who flew on such missions believed they fought for a just cause.

Nick Ferriman
Bangkok

SIR – The kindest explanation for Ariel Sharon's policy of “bash the Palestinians into submission” is to consider it a social experiment. To any outside observer, except perhaps George Bush, the experiment has failed.

When will Israeli and American leaders accept the evidence in front of them and start acting as politicians not generals?

Joe Lamb
Fife, Scotland

SIR – Your recent article on the security fence being erected between Israel and the Palestinian territories states that the hard core of the Israeli peace movement is opposed to it (“The passions aroused by terrorism, and by an anti-terrorism fence”, June 22nd). As an Israeli citizen who has voted for Meretz, one of Israel's most left-wing and pro-peace parties, for five straight elections, I assume you would place me in that hard-core category. Therefore, I would like to go on record as one of the overwhelming majority of Israelis who see this fence as an absolute security and political necessity. Palestinian terrorism has created a situation in which the only envisaged solution is a clear separation of the populations.

Mike Fainzilber
Israel

SIR – I applaud your leader highlighting the misguided nature of Cherie Blair's comments (“Hope and the suicide bombs”, June 22nd). However, it is wrong to imply that Yasser Arafat is, to use George Bush's term, “compromised by terror” solely because of his refusal to rein in Hamas since the Oslo accord.

The Karine-A seizure, as well as documents seized in “Operation Defensive Shield”, show that not only has Mr Arafat failed to rein in the terrorists, he is personally taking an active role in their funding and organisation.

We should expect Israel to talk peace with a Palestinian leader but only one who has firmly turned his back on terrorism. Mr Arafat has had many opportunities to become a statesman, but his refusal to change continues to delay peace and damage the interests of his people.

DARREN GOLD
London

SIR – Cherie Blair's remarks about Palestinian suicide bombers were just plain common sense: the outcry against her is hypocritical and politically motivated. There has been little sympathy for Palestinian victims of the Israeli army, with those casualties about three times as numerous and happening as a matter of daily routine.

You lecture the Palestinians on their failure to control the extremists, but perhaps some basic facts should be restated and kept in mind. Israel occupies the West Bank and, since the 1967 war, Israeli settlement there (and in the Gaza strip) has progressed continuously, regardless of the Oslo peace process. Israel is under a government which has done much to obstruct that process, by refusing to negotiate and trying to prevent the formation of a Palestinian state.

The same issue of *The Economist* contains a report on the real state of affairs in the West Bank (“Suffering for the crimes of the few”, June 22nd). It gives the Palestinian perspective, but with evidence provided by the Israeli human-rights group B'tselem. One reads there of 135 Israeli settlements, housing about 380,000 settlers, controlling 43% of the West Bank, with a buffer zone around them (closed to Palestinians) amounting to a further 20% of the West Bank. The Palestinian authority is consequently left with control over only 20% of its own territory.

M. Austin
University of St Andrews
Scotland

SIR – As someone whose Jerusalem living room directly faces Palestine—I live in pre-1967 Israel—my eyebrows rise every time I come across one of your testy critiques of the Israeli government's policy of self-defence. Yet, after reading your recent article ("The dirty bomber", June 15th), my eyes almost popped out.

Rightly so, but with no small measure of inconsistency, you describe the United States' new policy of pre-emptive intervention as a "sensible strategic shift". Understandably, to both your leader writer and to any sensible observer of the international scene, "America will in some cases strike before others strike it."

To quote an English proverb, surely you will agree that, "What's good for the goose is good for the gander."

A. Clarfield
Jerusalem

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Arab development

# Self-doomed to failure

Jul 4th 2002
From The Economist print edition

Alamy

**An unsparing new report by Arab scholars explains why their region lags behind so much of the world**

WHAT went wrong with the Arab world? Why is it so stuck behind the times? It is not an obviously unlucky region. Fatly endowed with oil, and with its people sharing a rich cultural, religious and linguistic heritage, it is faced neither with endemic poverty nor with ethnic conflict. It shook off its colonial or neo-colonial legacies long ago, and the countries that had revolutions should have had time to recover from them. But, with barely an exception, its autocratic rulers, whether presidents or kings, give up their authority only when they die; its elections are a sick joke; half its people are treated as lesser legal and economic beings, and more than half its young, burdened by joblessness and stifled by conservative religious tradition, are said to want to get out of the place as soon as they can.

Across dinner tables from Morocco to the Gulf, but above all in Egypt, the Arab world's natural leader, Arab intellectuals endlessly ask one another how and why things came to turn out in this unnecessarily bad way. A team of such scholars (it is indicative of the barriers to freely expressed thought that there are almost no worthwhile think-tanks in the Arab world) have now spent a year putting their experience to diagnostic use in the “Arab Human Development Report 2002”, published this week by the United Nations Development Programme (UNDP).

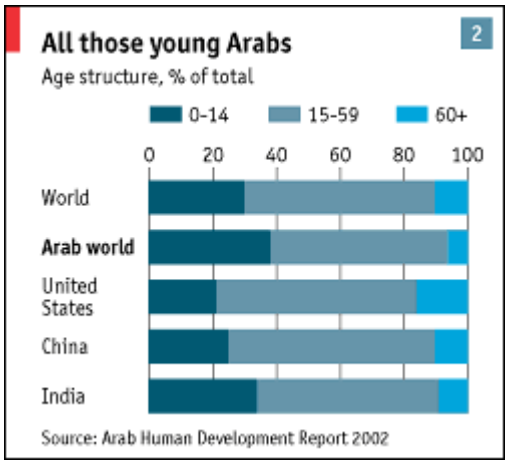
With Nader Fergany, an Egyptian sociologist, as the chief author, the report carefully dissects and analyses the Arab world's strengths and failings. The strengths, alas, consume little space; the failings are what interest the writers. Inbuilt caution holds them back from naming too many names, but they explain honestly and convincingly how and why they think their world has gone wrong.

For the past ten years, the UNDP's human-development reports and index (HDI) have been gauging a country's performance by its record in life expectancy, school enrolment and adult literacy as well as by its income per head. This is the programme's first comprehensive look at a separate region. The Arab survey is intended as an annual affair, with the first broad-brush approach to be followed by narrower reports, pin-pointing specific themes, such as the Arabs' failure to keep pace with the tumult of information and communication technology.

The Arab team has also produced a new index for the UNDP, the Alternative Human Development Index (AHDI). This excludes

income per head but adds measurements to the HDI that take account of a country's record on freedom, use of the Internet, and carbon-dioxide emissions. Predictably, the Arabs do even worse when they are measured this way.

The Arab world is taken to mean the 22 members of the Arab League, accounting at present for 280m people, or roughly the same as the United States, ranging from 68m in Egypt to 565,000 in Qatar. The region has the largest proportion of young people in the world—38% of Arabs are under 14—and it is calculated that the population will top 400m in 20 years' time.




There are good things to report: life expectancy has increased by 15 years over the past three decades, and infant mortality has dropped by two-thirds. Nor is it any surprise to be told that Arab income per head is higher than that in most other developing regions (though it is rather a surprise that its total GDP, at $531 billion, is less than Spain's). The Arabs have less abject poverty (defined as an income of less than $1 a day) than any other developing region, which is in part a tribute to Arab and Islamic traditions of charitable giving to the destitute. But, growls the report, “the region is richer than it is developed.”

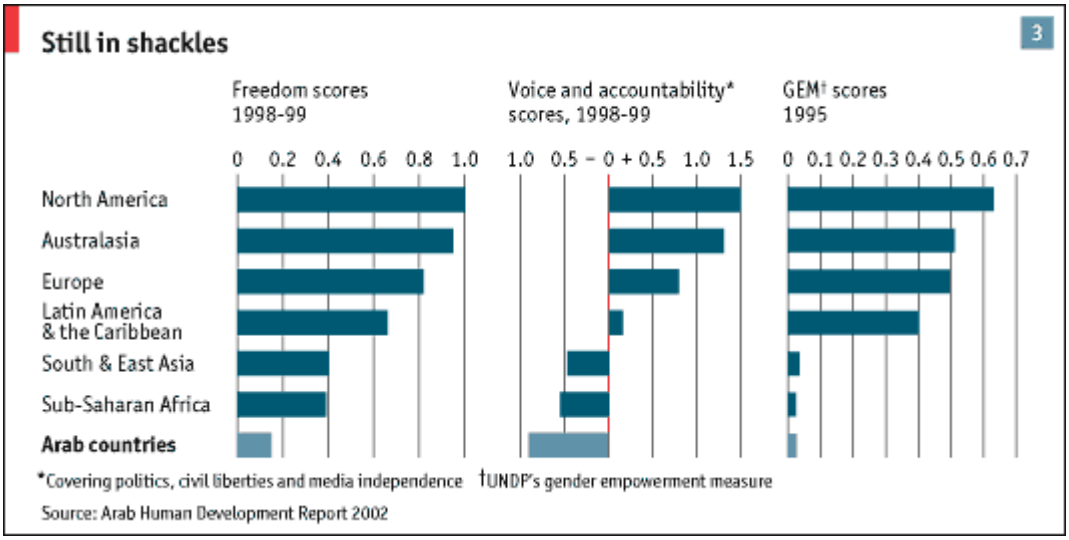
## Three things lacking

One in five Arabs still live on less than $2 a day. And, over the past 20 years, growth in income per head, at an annual rate of 0.5%, was lower than anywhere else in the world except sub-Saharan Africa. At this rate, says the report, it will take the average Arab 140 years to double his income, a target that some regions are set to reach in less than ten years. Stagnant growth, together with a fast-rising population, means vanishing jobs. Around 12m people, or 15% of the labour force, are already unemployed, and on present trends the number could rise to 25m by 2010.

The barrier to better Arab performance is not a lack of resources, concludes the report, but the lamentable shortage of three essentials: freedom, knowledge and womanpower. Not having enough of these amounts to what the authors call the region's three “deficits”. It is these deficits, they argue, that hold the frustrated Arabs back from reaching their potential—and allow the rest of the world both to despise and to fear a deadly combination of wealth and backwardness.

•**Freedom**. This deficit, in the UNDP's interpretation, explains many of the fundamental things that are wrong with the Arab world: the survival of absolute autocracies; the holding of bogus elections; confusion between the executive and the judiciary (the report points out the close linguistic link between the two in Arabic); constraints on the media and on civil society; and a patriarchal, intolerant, sometimes suffocating social environment.

The area is rich in all the outward trappings of democracy. Elections are held and human-rights conventions are signed. But the great wave of democratisation that has opened up so much of the world over the past 15 years seems to have left the Arabs untouched. Democracy is occasionally offered, but as a concession, not as a right.




“The transfer of power through the ballot box is not a common phenomenon in the Arab world,” the report says politely. Moreover, senior public servants, from ministers down, are seldom appointed solely on the basis of merit. People are given jobs not because of what they know, but because of whom they know. The result, all too often, is an unmoving, unresponsive central authority and an incompetent public administration.

Freedom of expression and freedom of association are both sharply limited. The report quotes Freedom House, an American-based monitor of political and civil rights, in recording that no Arab country has genuinely free media, and only three have “partly free”. The rest are not free.

Civil society, in the Arab world, has a terribly long way to go. NGOs are hobbled by legal and administrative obstacles laid in their path by authorities deeply suspicious of what they might be up to. But they also suffer from internal weaknesses, often getting their money either from foreign sources, which adds to the suspicions, or from the government, which defeats the object of their creation.

•**Knowledge**. “If God were to humiliate a human being,” wrote Imam Ali bin abi Taleb in the sixth century, “He would deny him knowledge.” Although the Arabs spend a higher percentage of GDP on education than any other developing region, it is not, it seems, well spent. The quality of education has deteriorated pitifully, and there is a severe mismatch between the labour market and the education system. Adult illiteracy rates have declined but are still very high: 65m adults are illiterate, almost two-thirds of them women. Some 10m children still have no schooling at all.

One of the gravest results of their poor education is that the Arabs, who once led the world in science, are dropping ever further behind in scientific research and in information technology. Investment in research and development is less than one-seventh of the world average. Only 0.6% of the population uses the Internet, and 1.2% have personal computers.

Another, no less grave, result is the dearth of creativity. The report comments sadly on the severe shortage of new writing, and, for instance, the decline in the film industry. Nor are foreign books much translated: in the 1,000 years since the reign of the Caliph Mamoun, say the authors, the Arabs have translated as many books as Spain translates in one year.

•**Women's status.** The one thing that every outsider knows about the Arab world is that it does not treat its women as full citizens. The report sees this as an awful waste: how can a society prosper when it stifles half its productive potential? After all, even though women's literacy rates have trebled in the past 30 years, one in every two Arab women still can neither read nor write. Their participation in their countries' political and economic life is the lowest in the world.

Governments and societies (and sometimes, as in Kuwait, societies and parliamentarians are more backward than their governments) vary in the degrees of bad treatment they mete out to women. But in nearly all Arab countries, women suffer from unequal citizenship and legal entitlements. The UNDP has a “gender-empowerment measure” which shows the Arabs near the bottom (according to this measure, sub-Saharan Africa ranks even worse). But the UN was able to measure only 14 of the 22 Arab states, since the necessary data were not available in the others. This, as the report says, speaks for itself, reflecting the general lack of concern in the region for women's desire to be allowed to get on.

## Why it all went wrong

A country can have one or two of these deficits, says Clovis Maksoud, a respected Lebanese involved in the report's preparation, and still surge ahead. Singapore, for instance, manages to prosper without offering much political freedom. It is when a country or a region suffers from all three deficits that it is in such a bad way.

There are no clear historical reasons why it has turned out like this. The priority, in the years after the second world war, was to get rid of the western powers that were still ruling much of the region either directly or through proxies. The emphasis was on national liberation, not on individual liberty. Nationalism was drummed into people, leaving little room for thoughts of personal freedom.

But when the imperialists were gone, the new independent governments often aped their old colonial administrations (not the European governments behind these administrations) by adopting their characteristics of extreme centralisation, very little separation of power between different branches of government, and a generally paternalistic attitude. The late Anwar Sadat even used to address the Egyptian people as “my children”.

The Arab authors of the survey avoid making the Arab-Israeli conflict either a cause of, or an excuse for, their region's failings. The report contains references to the particular circumstances of the Palestinians living under occupation or as refugees, and its overview has a section that refers to the pall cast by the conflict over the political and economic life of the entire region. And, indeed, the business with Israel, in particular Israel's occupation of Palestine, is a severe distraction. It absorbs much-needed energy, and its effect is to turn people's thoughts, yet again, from individual liberty to national liberation.

Blaming outside intervention for the region's sorrows is not as fashionable as it was during the cold war. But it still has some validity. Since September 11th, for instance, outside events have provided authoritarian rulers with an excuse to get away with doing some pretty nasty things, particularly if done to Islamist dissidents. Syria, for instance, is usually prominent on America's list of outcast states. But right now its security services are engaged in questioning an alleged al-Qaeda leader under torture, with America's tacit approval and encouragement.

Restrained about Israel, the report has other, no doubt less voluntary, constraints. The Arab countries are a remarkably heterogeneous lot. Little, for instance, links secular Tunisia and Islamic Saudi Arabia except for their common refusal to give a dissident voice a hearing. But the report—and this is both its strength and its weakness—takes the region as a whole, seldom differentiating between countries.

The tables at the end give the game away by showing how individual Arab states are ranked on several delicate issues. But the text studiously avoids specificity, except to point out where some country or other is doing rather better. It is remarked upon, for instance, that Kuwait and Qatar have allowed reasonably free elections to national assemblies, and that Jordan and Egypt have made advances towards equality of the sexes (but see this article for Jordan's back-treading on democracy and civil rights).

## Do not search or question

The most delicate issue of all, again carefully skirted by the authors of the report, is the part that Islam plays in delaying and impeding the Arab world's advance towards the ever-receding renaissance that its intellectuals crave. One of the report's signed articles explains Islam's support for justice, peace, tolerance, equilibrium and all good things besides. But most secularists believe that the pervasive Islamisation of society, which in several Arab countries has largely replaced the frightening militancy of the 1980s and early 1990s, has played a significant part in stifling constructive Arab thought.

From their schooldays onwards, Arabs are instructed that they should not defy tradition, that they should respect authority, that truth should be sought in the text and not in experience. Fear of *fawda* (chaos) and *fitna* (schism) are deeply engrained in much Arab-Islamic teaching. “The role of thought”, wrote a Syrian intellectual “is to explain and transmit...and not to search and question.”

Such tenets never held back the great Arab astronomers and mathematicians of the Middle Ages. But now, it seems, they hold sway, discouraging critical thought and innovation and helping to produce a

great army of young Arabs, jobless, unskilled and embittered, cut off from changing their own societies by democratic means. Islam at least offers them a little self-respect. With so many paths closed to them, some are now turning their dangerous anger on the western world.

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Jordan's democratic freeze

# The king knows best

Jul 4th 2002 | AMMAN
From The Economist print edition

## Retreating from glasnost

Get article background

AP

**Faisal fights her corner**

ALMOST alone in this muzzled region, Jordan, for a time, held out a glimmer of hope. And it still all looks pretty good to a visitor; the immigration police, for instance, wave through Iraqi and Israeli passport-holders alike. But Jordanians say that a decade of cautious *glasnost* is now being reversed.

Over the past two years, human-rights groups have counted 80 new temporary laws decreed by King Abdullah. Under changes to the penal code, for instance, unauthorised public meetings are banned and the authorities can now imprison journalists "for sowing the seeds of hatred". The decrees can be reversed by parliament, but parliament has been dissolved.

Nor has any date been set for elections, already delayed for a year. The king says more time is needed to issue magnetic identity cards. But he adds that "If I want to change a government, I do it for the better; otherwise it is better to keep the one I know."

As always, September 11th is the pretext. The Americans, pushing hard for electoral change in Palestine, across the Jordan river, have been mute about the democratic freeze on the river's east bank. Jordanians are inclined to take this as an endorsement.

Islamists have been detained in hundreds. And the net has stretched wider. In May, Toujan Faisal, the kingdom's first female member of parliament, was sentenced by the State Security Court to 18 months in prison, for an article on the Internet that accused the prime minister of profiting from a decree doubling car-insurance rates.

Ms Faisal's case won support that ranged from former prime ministers to Islamists, whose newspaper, *Sabil*, for the first time backed a female politician. After three months in prison, the king last week decreed her pardoned of her conviction, though not of her crime. Ms Faisal is now receiving well-wishers she hopes to turn into a new political force.

Officials say that the new security measures are the price for stability in troubled times. Palestinian-born Jordanians, who comprise the majority, are restless at what they see as the king's lack of support for their kin. Jordanian Islamists are said to have returned from Afghanistan to plot attacks on western targets. Even so, it is a worry that the king has nobody to counter-balance the advice he gets from his intelligence men.

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Corporate scandals and politics

# The backlash against business

Jul 4th 2002 | WASHINGTON, DC
From The Economist print edition

**Corporate malfeasance is on the verge of becoming a big political issue—even though the public hardly cares about it yet**

DOMESTIC matters have failed to exert much of a hold on American politics since the destruction of the World Trade Centre. The vanishing budget surplus, campaign-finance reform and the rest have come and gone, leaving not a wrack behind. Yet disintegrating confidence in corporate America will surely be different. This week, it reached even the door of George Bush himself.

Following the revelation that worthless WorldCom had padded its accounts to the tune of $3.9 billion—which itself followed a series of other scandals dating back to the collapse of Enron—Mr Bush put himself at the head of a parade of outrage demanding a measure of responsibility from corporate executives. He interrupted the G8 summit in Canada to complain about balance-sheet shenanigans. He gave a radio address demanding that executives should be criminally liable if they give intentionally misleading information. Next week he will give a big speech on Wall Street to explain more policies.

His rhetoric already marks a change. After the Enron affair, Mr Bush talked about a few “bad apples”. Now he is talking about threats to “our entire free enterprise system”. His change was necessary not just because of the mess (to suffer one business scandal may be regarded as a misfortune; to suffer eight looks worse than careless), but also because the scandals have dangerously reinforced the idea that Republicans are soft on business.

Although the WorldCom affair has nothing to do with political corruption (the company did not seek government help, as Enron did), it certainly smacks of corporate corruption. That is the stick Democrats are beating Republicans with. They sneer that the president's rhetoric about tackling white-collar fraud is belied by his earlier reluctance to give the Securities and Exchange Commission (SEC) more money. The leader of the Senate, Tom Daschle, has incredulously contrasted the Republicans' current outrage with their earlier deregulatory fervour. Most alarmingly, eyes are turning to the president's own business record. The SEC investigated some of his share dealings in 1990-91, when Mr Bush, then on the board of Harken Energy Corporation, took 34 weeks to give “timely” notice of an $848,560 stock trade, made a week before bad news was disclosed.

The outrage has already revived a bill on accountancy reform that had appeared dead in the Senate only two months ago. The bill, sponsored by Paul Sarbanes, a Democrat from Maryland, would create an

independent regulatory board to set book-keeping standards, limit accountants' consultancy work, discipline dodgy auditors and prevent a senior auditor from working with a public company for more than five years. Mr Daschle says the Senate will vote on the bill next week and forecasts it will pass by a landslide.

Weirdly, the outrage in Washington is not matched by any surge in public opinion about the issue. There are some signs of change. Mr Bush's ratings for handling the economy have begun to fall, from 60% in January to 53% now. Polls also show rising concern about the quality of financial information. In March, a third of respondents thought the problem was confined to a few isolated cases—the “bad apples” theory. Now fewer than a quarter do, and at least two-thirds say they think most companies tell lies. Talk radio, cable television and other barometers of grass-roots political opinion have become incensed.

On the other hand, Mr Bush's overall ratings remain stratospheric. A poll by Stan Greenberg (a former adviser to Al Gore) found people still think Republicans do a better job of handling the economy than Democrats, though they trust Democrats more to crack down on fraud.

Corporate ethics hardly figures in the mid-term elections yet. True, the fiercely competitive race in Mississippi's third district has become a battle of blame between Chip Pickering, the Republican incumbent, and Ronnie Shows, a congressman from a neighbouring district who accuses Mr Pickering of being too close to the disgraced WorldCom, which is based in the district. But that is a special case. Elsewhere, corporate ethics ranks well below other issues.

Karlyn Bowman, an observer of social trends at the American Enterprise Institute (AEI), argues there has been no break in the overall pattern of attitudes to business as a whole. For the past 20 years, 55-65% of the country has expressed “some confidence” in those running big businesses; 10-25% express a great deal of confidence. The numbers are now towards the lower end of those ranges—a decline in confidence, but no backlash against business.

**Is the current business-bashing in Washington just a short-term craze?**

So is the current business-bashing in Washington just a short-term craze? It is possible. The economy still looks reasonably healthy. Share prices are falling, but still hover above the point at which Alan Greenspan worried about “irrational exuberance”. The bubble is deflating rather than bursting. Meanwhile, both sides have political reasons of their own for not ramping up the rhetoric much further. The White House has to balance the need for good business ethics against the risk of panicking the markets. The Democrats fear regaining their reputation, so painstakingly shrugged off in the Clinton era, of being hostile to business.

That said, there are reasons for thinking the worries about corporate America will not conveniently go away. To begin with, there may be a lag in the public response. The scandals at WorldCom, Adelphia, Tyco and the rest may simply be too recent to have had their full effect yet.

Next, it is almost impossible to believe that all the bad business news has now come out. Most of the misbehaviour seems to be related in some way to the huge incentives Wall Street provided in the past decade for reporting rising earnings quarter after quarter (or rather, earnings that exceeded ever-rising expectations). The half dozen firms which responded to this incentive by cooking their books cannot be the only ones. The likelihood is that many more will emerge: as Norm Ornstein of the AEI points out, public prosecutors and the press have incentives of their own to find more malefactors of great wealth.

And if so, that would surely affect America's electoral politics. Bill McInturff, the head of a Republican polling outfit, Public Opinion Strategies, argues that over time a president's approval rating is generally about 20 percentage points above the number of people saying the country is on the right track, which in turn is strongly influenced by consumer confidence. At the moment, Mr Bush's 70% standing is both exceptionally high and 20 points above the right-track question. Since 1945, only three presidents have approached this sort of approval just before a mid-term election, and their parties did well in all of them. But consumer confidence, as measured by the University of Michigan index, fell almost 4.5 points in June.

A few more corporate scandals and a further decline in the stockmarket and the dollar could well push down both the right-track measure and Mr Bush's standing. At that point, the Republicans would be in real trouble. The economy, too.

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**The retirement of J.C. Watts**

# Ave atque vale

Jul 4th 2002 | WASHINGTON, DC
From The Economist print edition

**A black Caesar meets his Ides of July. Was Tom DeLay his Brutus?**

GEORGE BUSH spent the week trying to put the compassion back into his conservatism, speaking about school vouchers in Cleveland and welfare reform in Milwaukee. Back in Washington, DC, the “compassion agenda” suffered a blow.

On July 1st, J.C. Watts, the only black in the Republican caucus, announced that he plans to retire in November. Mr Watts, whose initials stand rather wonderfully for Julius Caesar, was the poster-boy of Mr Bush's inclusive Republicanism: a star university quarterback who became chairman of the House Republican Conference, the fourth-highest office-holder in the congressional hierarchy.

The Republicans wheeled out the articulate Mr Watts whenever they needed to show a bit of diversity. He delivered the rebuttal to Bill Clinton's state-of-the-union address in 1997. Mr Bush gave him a leading role in his multicultural convention in 2000. None of the six black Republicans running for election this year stands much of a chance. (The Democratic caucus currently has 38 blacks, though none are in leadership positions.)

**A party once keen on term limits is now painfully aware of the value of incumbency**

Why is he going? Mr Watts gives family reasons—he has a wife and five children. And commuting between Oklahoma and Washington is a pain. A forthcoming book, “What Colour is a Conservative?”, may give him a chance to launch a new career as a black Bill Bennett, the man who went from being Ronald Reagan's education secretary to becoming a watchdog of “American values”.

But there are also political reasons for his departure. Mr Watts, who was first elected to Congress in 1994 as part of Newt Gingrich's conservative revolution, lost a power struggle with Tom DeLay, the majority whip (and number three in the hierarchy). Mr DeLay has sewn up his accession to the number-two position, the majority leadership, which is being vacated by Dick Armey's imminent retirement; and he also seems to have made sure that his current job will go to one of his lieutenants, Roy Blunt, not Mr Watts.

Mr Watts is also bitter about the administration's decision to discontinue the Crusader, an army gun which is made in his constituency. He is angry that the Bush administration singularly failed to consult him or give him warning of the decision.

Mr Watts's retirement will spark off one of the fiercest congressional battles in the country. Although he would have walked into his fifth term, his district—Oklahoma's third—is a classic swing seat: known as “little Dixie” because of its historically high Democratic registration, but increasingly drifting towards the Republican camp.

Mr Watts is not the only high-profile Republican who is leaving. The departure from the Senate of Strom Thurmond (99) and Jesse Helms (80) may have been predictable. But the Republicans have been shaken by the fact that Phil Gramm and Fred Thompson, too, are leaving the Senate, and Dick Armey the House. A party once keen on term limits is now painfully aware of the value of incumbency.

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The International Criminal Court

# Right to the brink

Jul 4th 2002
From The Economist print edition

**A last-minute reprieve at the UN, but no end to hostilities**

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AP

**Just don't foul anybody deliberately**

HARD cases provoke hard words. The United States rejects the jurisdiction of the International Criminal Court (ICC), and wants its European allies to know it. By vetoing the extension of the United Nations mission in Bosnia, said America's UN ambassador, John Negroponte, America was demonstrating “just how serious our concerns remain” about the “more than perplexing” refusal of other countries to grant American and other peacekeepers on UN operations immunity from prosecution by the court. That was tantamount to “taking hostage the operation in Bosnia”, retorted Javier Solana, the European Union's foreign-policy chief.

Just as a temporary extension to the UN mandate was due to run out on July 3rd, efforts to reach a compromise foundered and both sides agreed to another 12-day breather. Even if an agreement is eventually reached, the episode has shaken America's European allies. How far is the Bush administration willing to go to try to kill the court? And how committed is it, really, to international peacekeeping?

After the brinkmanship at the UN this week, the answer to the first question, at least, seems pretty clear: the American government is willing to go much further than its allies had expected. The immediate effect of a failure to renew the UN mandate in Bosnia would have been awkward, but not a catastrophe. The European Union would have had to scramble to take over a 1,500-strong UN force that is training local police, a handover which is planned for January anyway. Even an American withdrawal from all UN peacekeeping operations would not have been an operational disaster. Just 46 American police are working under a direct UN mandate in Bosnia, and the United States has only 700 or so people serving in UN peacekeeping missions worldwide.

However, America has not threatened to withdraw its personnel from UN missions. It has threatened to veto, one by one, the missions themselves. In fact, most American troops abroad, including those in the Balkans, do not operate under UN mandates. Nevertheless, an American veto of UN peacekeeping would create huge headaches for its allies, and undermine the whole concept of international peacekeeping generally.

In a letter this week to Colin Powell, America's secretary of state, Kofi Annan, the UN general secretary, complained that America's demand “flies in the face of treaty law” and risks bringing discredit to the Security Council itself. Even if this particular quarrel can be patched up, America's allies must now know it is not the end of the story. Some Bush officials not only think the creation of the court was misguided, they loathe it as a prime example of international agreements which could, some day and in some context, constrain America's freedom of action.

One irony is that most of America's detailed objections to the court have been accepted. Many of America's allies, including Britain and France, fellow permanent members of the Security Council and also involved in peacekeeping, shared America's fears of a rogue court. They also wished to avoid precisely what they now face—unrelenting American hostility to the ICC. When Bill Clinton was in the White House, accommodation seemed a reasonable hope. The Clinton administration opposed the ICC treaty, but its negotiators played a key role in its drafting and, just as important, the formulation of the detailed rules for the court's operation. George Bush put a stop to that in May.

## It can already escape

The truth of the matter, an awkward fact for both the Europeans and the United States, is that Mr Clinton's negotiators succeeded in inserting so many loopholes into the ICC treaty and the court's rules that American personnel now have de facto immunity. One loophole, which the Bush administration will exploit to the full, leaves intact the bilateral military agreements America has with more than 100 countries, which give America exclusive legal jurisdiction over its soldiers and officials. These cannot be breached by the ICC. On top of that, they can probably be amended explicitly to exclude ICC jurisdiction (lawyers argue about this, but America is likely to win).

Moreover, American negotiators played a key role in writing the “elements of crimes” that fall within the remit of the ICC. These cover only “widespread and systematic” atrocities—bombing Afghan weddings by mistake does not qualify. In any case, an atrocity must first be investigated by national authorities. Only if a national government refuses to investigate or prosecute, or mounts a sham trial as a whitewash (Saddam Hussein can't simply acquit himself), would the ICC be able to act. American accusations that the ICC's prosecutor will pursue Americans despite all these obstacles seem wildly exaggerated. The prosecutor cannot open an investigation without the approval of a three-judge panel. If the prosecutor and the judges all go berserk, the countries that have joined the court (most of them America's allies) can remove them.

The purpose of the ICC is to provide a permanent forum to put on trial the likes of Pol Pot and Mr Hussein, not Americans or, for that matter, Europeans. In fact, many developing countries have signed up to the court precisely to gain some legal protection against such monsters. But the Europeans argue that, for the court to make a credible claim to even-handedness, no one can be guaranteed a permanent blanket immunity from its reach. Nearly all America's NATO allies are willing to take the infinitesimal risk that this entails. So far, the Bush administration is not.

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Troubled youth

# Band on the run

Jul 4th 2002 | DES MOINES
From The Economist print edition

**Why do more teenagers seem to be running away from home?**

EVERY NIGHT, a van cruises the city streets, searching parks and abandoned buildings for runaways and homeless youths. Volunteers implore the adolescents they find to seek shelter. Failing that, they offer “survival packets” and free telephone calls. This is not Rio de Janeiro or Calcutta. It is Des Moines, Iowa.

**Hoofing it**
Mid-west homeless adolescents, %

| Victims of being: | |
|---|---|
| threatened with a weapon | 48.2 |
| asked to do something sexual | 33.0 |
| beaten up | 32.7 |
| robbed | 27.2 |
| **Living in:** | |
| shelter or mission | 40.2 |
| foster/group home | 15.8 |
| friend's home | 15.6 |
| relative's home | 10.5 |

Source: Mid-west Longitudinal Study of Homeless Adolescents

Some 7,000 young people ran away from home in Iowa last year. (For the incident to be counted, a missing-person report must be filed with the police.) Most of those fleeing adolescents returned home within 24 hours; many did not. Around 200 young people are living on the streets of Des Moines at any one time, reckons George Belitsos, the executive director of Youth and Shelter Services, a non-profit group. His organisation has offered shelter to 453 young people over the past 12 months. Half are runaways and half are homeless. What is the difference? “They become homeless because nobody's looking for them any more,” says Mr Belitsos.

Of course, Iowa is no different from the rest of the country. The National Network for Youth reports that 2.8m youths had what it euphemistically calls “a runaway experience” during the previous year. It is hard to say how many of these runaways spent long spells on the street. Les Whitbeck, a University of Nebraska sociologist, reckons that counting the adolescent homeless is like trying to count flies in a room with the door and windows open. Many runaways don't want to be found, and, Mr Whitbeck says, they look little different from other children.

Looks deceive, however. Mr Whitbeck is part of a team from the University of Nebraska that recently produced the Mid-west Longitudinal Study of Homeless Adolescents (MLSHA), based on interviews with 455 runaway adolescents in eight mid-western cities. The research, which began in 2000, with follow-up interviews every three months, paints a portrait of deeply troubled young people who leave home because they have been abused, only to find life on the streets often worse.

Roughly half of the boys and a third of the girls in the study suffer from “conduct disorder”, a mental illness associated with emotional problems, compared with 10% among all teenagers. Some 16% were thrown out of home; more left because they were sexually or physically abused. Nearly three-quarters of all runaways say they have been struck with some hard object; a quarter of the girls have been asked to do something sexual. Some 23% of the males and 43% of females show signs of post-traumatic stress disorder.

Life on the street is rotten, too. A third of the subjects surveyed in the MLSHA have been beaten up; nearly half have been threatened with a weapon. Runaways are far more likely to engage in risky teenage behaviour: drugs, alcohol, unprotected sex. Nearly half of the girls interviewed had been pregnant at least once. With no means of support, homeless youths are also more likely to steal, deal in drugs or trade sex for a place to stay. Half the teenagers in the study have thought of killing themselves in the past 12 months.

Why do more American boys and girls appear to be fleeing from home? Economic problems often play a role, despite the generally healthy state of the American economy until relatively recently. One in three of the young people turning up at Iowa shelters report that one of their parents is unemployed. A more fundamental problem is the shaky state of the American family. The rise in the number of single-parent

families over the past quarter of a century has meant that more kids fall through the cracks of divorce. And weaker family ties mean that fewer troubled teenagers find refuge with a kindly grandparent or uncle.

When it is possible (and safe), the runaway groups try to reunite children with their families. But a large number of runaways show no sign of wanting to go back: the average adolescent who turns up at an Iowa shelter has run away more than six times. The only way to deal with such chronic runaways is to treat them as “too early adults”, argues Mr Whitbeck. That means offering them shelter and drop-in facilities and teaching them about jobs and living alone. “They simply won't go back to being children again,” he says.

Of course, it would be preferable to raise healthier children in the first place. That not-so-simple task would begin with parents learning to behave better. If that doesn't happen, the wish-list includes earlier intervention by schools, more money for counselling, better drug treatment—indeed, anything that will bring responsible, caring adults into the lives of troubled young people. Without such help, the iron law of so many social problems will prevail. Deeply troubled families all too often produce deeply troubled children.

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Recycling

# Waste of time

Jul 4th 2002 | NEW YORK
From The Economist print edition

**New York's budget punctures a costly green fantasy**

NINE years ago, with much fanfare, Rudy Giuliani set up a recycling programme whereby New Yorkers had to separate their rubbish into its different elements before it got collected. Millions of dollars were spent on the advertising campaign. Righteous citizens, at the mayor's bidding, and under threat of being fined, duly separated plastic from metal, glass from paper, using colour-coded bin bags. At a cost of $40m a year, garbage trucks made special runs to pick up the various loads.

It was all very worthy. There was, however, a small problem: the lack of demand for recycled glass and plastic meant that a much of the rubbish destined for recycling ended up in a landfill, just like the rest of the city's waste.

This expensive operation might well have continued were it not for New York's fiscal crunch. Battling for every dollar, the new mayor, Michael Bloomberg, this week suspended the glass-and-plastic part of the programme. Howls of protest followed. The mayor got his way only after reluctant city councillors asked themselves what other cuts could save as much money without doing more harm.

Environmentalists say this is the first serious rollback of a recycling programme in the United States. More may follow, since state and city governments almost everywhere face a financial squeeze. Half of the country does some sort of recycling, and presumably most of it, like New York's, is done at considerable expense. In 1990, recycling diverted some 34m tonnes of rubbish away from landfills and incinerators. By the end of the 1990s, that had gone up to 64m tonnes. But at what cost to the taxpayer?

Mr Bloomberg says he is just being practical. Under Mr Giuliani, the cost of waste-disposal soared—thanks in part to Mr Giuliani himself, who closed the city's one landfill and, lacking an adequate replacement nearby, added $500m a year to the city's budget to cart the trash 500 miles away. Mr Bloomberg might have been stuck with the problem had he not found a loophole that allows the abandonment of a recycling plan if there is no market for the goods.

This sensible decision earned Mr Bloomberg a bashing from the New York media, which he readily admits to loathing. (He also got into trouble this week for joking that the police now have enough weapons to “blow away the press”.) He had better get used to it. With a likely budget deficit of at least $5 billion in each of the next two or three years, New York will have to cut services that do far more useful things than deluding the city's greens into thinking they are making a difference.

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Training doctors

# Too little money, too much paper

Jul 4th 2002
From The Economist print edition

**Medical education is in pain**

THE true physician, said Plato, is not a mere moneymaker. America's well-off doctors would heartily agree—and not just because (as Plato explained) their minds are on their patients' welfare. Today's doctors too often feel like over-worked clerks. They have to slog their way through a nightmarish jungle of insurance claims and other paperwork.

That is part of the reason why the number of Americans wanting to go to medical college has fallen for five years in a row. Some of the decline can be chalked up to the past decade's economic boom, when other work looked so much more lucrative. But a lot of potential doctors have been put off by horror stories of graduates who work 100 high-stress hours a week at training hospitals for a mere $40,000 a year, after piling up an average of $100,000 in medical-school debt. And then, having finished their training, doctors find themselves facing a mountain of administrative work. Other professions, notably the law, have recently halted the decline in their applicant numbers; but medicine is still on the skids.

Jordan Cohen, president of the Association of American Medical Colleges (AAMC), says that medical colleges are still getting a reasonable number of good students. The AAMC has a more pressing worry: money. Most teaching hospitals (where students do resident-work for at least three years) get their money mainly from the federal and state governments, plus doctors' fees and undergraduate students' tuition fees. These days they are hard up. According to Robert Dickler, the AAMC's senior vice-president, between 25% and 30% of the big teaching hospitals are losing money each quarter.

This is partly because teaching hospitals are expensive to run: teaching costs money, and teaching hospitals also tend to treat more uninsured patients, and do more specialised surgery, than regular hospitals. They also do a lot of research, the cost of which is rising fast, despite generous injections of cash from the National Institutes of Health. There is less money than ever to pay for all this: teaching hospitals' budgets have been squeezed by the managed-care system, which has cut the price and frequency of services such as diagnostic tests, and by the scrimping imposed by the 1997 balanced-budget act. So far, says Mr Dickler, most have managed to scrape by; but they may not be able to do so much longer.

As money gets tighter, teaching gets shorter shrift. A recent study by the Commonwealth Fund Task Force on Academic Health Centres showed that teaching hospitals don't do nearly as much teaching as they should. Patients are hustled out of hospitals sooner—partly because of surgery's technological advances—and this deprives students of the chance to learn follow-up care. Teachers have less time to teach; their pay cheques come mostly from clinical care, not from teaching. Earnings from clinical care also help to pay for other hospital activities, such as research, so Medicare's slashing of doctors' pay (by more than 5% this year) hurts.

Money worries at teaching hospitals could get even worse as resident students clamour for better conditions. Last month the Accreditation Council for Graduate Medical Education decreed an 80-hour-a-week cap on residents' work hours; this will probably mean poorer service for patients. In May, several doctors filed an anti-trust lawsuit claiming that the National Matching System—which single-handedly assigns all medical-school graduates to their residencies—keeps wages unfairly low and hours horribly long. All very well to complain, says Mr Cohen, whose organisation is among the suit's defendants: but what, save chaos, is the alternative?

The medical establishment is creakily tackling its host of problems. Urged on by the AAMC, many colleges are vigorously trying to recruit more non-white, non-Asian students (currently a dismal minority). Some of them, such as Brown University, have set up partnerships with colleges in non-white areas, and go

trawling for students there.

But the money problems are harder to fix. Some institutions are merging. Most have done painful cost-cutting, slicing down their administrative staffs. A few have closed; the largest of these was Mount Sinai Hospital in Cleveland, two years ago. And come October, medical education could lose yet more money from cuts in indirect Medicare payments. The profession is not in a healthy state.

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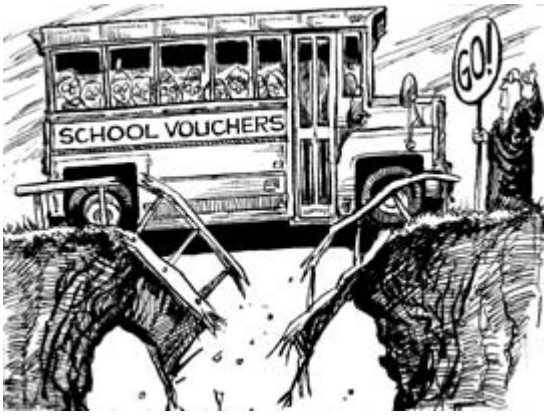
Lexington

# Inching towards reform

Jul 4th 2002
From The Economist print edition

**But school vouchers, alas, still face a tough battle to win acceptance**

Get article background




SUPPORTERS of school vouchers, which give parents the chance to choose where their children go to school, are walking on air. For years the education establishment has been arguing that one of the biggest school-voucher programmes in the country—in Cleveland, Ohio—violates the constitution's separation of church and state because virtually all the parents use their vouchers to send their children to religious schools. On June 27th, by a five-to-four majority, the Supreme Court disagreed: so long as the parents are doing the choosing, it argued, it does not matter if the money ends up in religious schools.

The voucher movement celebrated in the best way possible—by going on the offensive. Within hours of the ruling, Richard Armey, a Republican congressman from Texas, introduced a law to create an experimental voucher programme in Washington, DC, one of the country's worst school districts. There are also plans for similar bills in Virginia, Texas and Colorado.

It is time to come down to earth. Persuading five judges to remove a constitutional impediment to school choice is one thing. Persuading the country at large to embrace a little-understood idea will be quite another—not least because it requires a war with one of the most powerful forces in American politics.

America's two big teachers' unions have a combined membership of about 3.5m people, a political war chest of more than $1 billion a year, a hardened corps of spin doctors and a vast army of busybodies. They are willing to do almost anything to destroy vouchers, which they regard as a mortal threat to their well-being. A couple of years ago a union lawyer promised that, whatever the Supreme Court decided, his organisation would still fight school choice “on whatever grounds are available to us—from lofty principles to ‘Mickey Mouse' procedural issues”.

It is only a small exaggeration to describe the Democratic Party as a wholly-owned subsidiary of the teachers' unions. Throw a brick into any large gathering of Democrats and you are sure to hit a teacher or two. It is impossible to win a nomination for national office without pledging allegiance to the unions on vouchers. Politicians who have erred (foolishly led astray by the patently ridiculous idea that they are supposed to look for ways to improve schools) have rapidly been strong-armed back into the fold: witness the craven retractions by Joe Lieberman and Bill Bradley before the 2000 election.

This means that the job of championing vouchers falls by default to the Republicans. But Republicans are hardly the ideal champions for a measure that primarily benefits poor blacks in the inner cities—not least because their own base, the middle-class suburbs, are perfectly happy with their local schools (which are often the reason why they live where they do). Very few think “their” schools really need a large influx of poor black children using vouchers to flee from inner-city schools.

So far the only three voucher schemes to get off the ground—in the cities of Cleveland and Milwaukee and a statewide one in Florida—have all required the whole-hearted support of the Republican establishment (which they got in all three states). They have also usually needed street-level campaigns by inner-city supporters. Milwaukee and Cleveland would never have got the chance to experiment without the tireless work of poor black mothers who rallied their friends to protest.

Even when the Republicans and inner-city leaders combine, the teachers' unions still have two lines of defence. The first is public opinion. Discontent with schools is concentrated in the inner cities: most Americans claim to like their schools and trust their children's teachers. It is much easier to scare people into resisting change than it is to persuade them to support experimentation. The two voucher initiatives on the ballot in November 2000—in California and Michigan—both lost by huge margins, thanks largely to a negative advertising blitz financed by the teachers' unions. In the past two years as many as 28 state legislatures have rejected voucher schemes of one sort or another.

The second line of defence is legal. The Supreme Court has not necessarily had the last word on this subject. As many as three dozen states have constitutions that are even stricter about the separation of church and state than the federal constitution; some specifically ban states from giving money to religious schools. Supporters of vouchers are confident that they will be able to challenge these restrictions on the basis of the equal-protection clause of the constitution. But state constitutions nevertheless provide the unions with just the sort of “Mickey Mouse” issues that could hold vouchers at bay for years to come.

## Once more into the breach

Which is not to say that the Supreme Court's ruling changes nothing. The simple fact that the voucher experiment has been allowed to continue is an enormous victory in itself. The longer the experiment continues, the harder it will be for the teachers' unions to claim that competition destroys public schools (which it patently has not done so far). With each positive result, inner-city minorities will be ever less willing to accept the status quo. Blacks with school-age children already support vouchers by a majority of three to one.

The Supreme Court did more than allow vouchers to survive. It gave the movement a new energy. George Bush has hitherto treated vouchers as a little too hot to handle. But this week he went to Cleveland to celebrate the court's decision, which he compared with *Brown v Board of Education*, the landmark 1954 ruling that ended school segregation.

It was an apt comparison. There is no doubt that the teachers' unions will be able to blunt the impact of the court's decision, just as the segregationists did in the wake of *Brown v Board of Education*. But nor is there any doubt that America's future lies with the people who are trying to expand opportunity rather than those who are trying to bar the schoolroom door.

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**Bolivia's election**

# Desperate for change—and for more of the same

Jul 4th 2002 | LA PAZ
From The Economist print edition

Reuters

**A free-market president and a strident leftist opposition ready to take to the streets: Bolivia's election result may spell trouble**

Get article background

RIGHT up to polling day, it seemed that Bolivians would fall for the charmer. Manfred Reyes Villa, a slick former soldier with a handsome moustache, promised to dump the free-market "neoliberal" policies that South America's poorest country has followed for the past 15 years and embark on a spending spree to boost the economy. But as results trickled out after June 30th's vote, Mr Reyes found himself neck-and-neck with the very embodiment of such IMF-inspired policies: ex-president Gonzalo ("Goni") Sanchez de Lozada, a grizzled, American-educated businessman with a thick gringo accent, whose 1993-97 administration pushed through privatisations and other liberal reforms. With almost all votes counted, both candidates had around 22%.

Faced with a choice of 11 parties, each with its own presidential candidate, Bolivians seem to have voted both for radical change and for more of the same. Most votes were shared among candidates who promised a rupture, including Evo Morales, the hard-left leader of Bolivia's *cocaleros* (coca growers), who campaigned against the American-backed policy of eradicating coca plantations and was closing fast on the leaders with a surprising 21%. And yet Bolivians gave Mr Sanchez's misleadingly named Nationalist Revolutionary Movement (MNR) more seats in Congress than any other party, though not a majority.

Under Bolivia's constitution, since no presidential candidate got 50% of the popular vote, the new Congress will convene in early August to choose between the two front-runners. Of them, Mr Sanchez is more likely to build a big enough coalition to secure the presidency and govern thereafter, especially if he wins the support of ex-president (1989-93) Jaime Paz Zamora of the Movement of the Revolutionary Left, who came fourth. Mr Paz, though he attacks free-marketry, seems happy to sacrifice his socialist principles for a slice of power, as he did when he joined the government of Hugo Banzer, an ex-dictator turned democrat, in 1997.

Mr Reyes and his populist New Republican Force refused to accept defeat, seeking a coalition with Mr Morales's Movement to Socialism. Mr Morales would have none of it. He clearly sees his future role as that of opposition leader—in Congress and, if that doesn't bring results, back on the streets where his movement began as an uprising against the deepening of rural poverty caused by the anti-coca programme. In the final days of the campaign, America's ambassador clumsily warned voters that the foreign loans and aid that Bolivia depends on might be stopped if Mr Morales's group gained power. He also said Bolivia's access to the United States market, its main export customer, would be at risk. To Mr Morales's joy, many Bolivians gave him their vote in protest.

The coca-eradication programme, and the economic troubles among Bolivia's neighbours, have cut the country's annual growth rate from the 5% seen in the mid-1990s to only 1.2% last year. Since the population is growing twice as fast, that means national income per head fell in a country where two out of three people already live in poverty. Weak growth, a lack of spending restraint and a bungled pensions reform have sent the government's deficit soaring to a probable 6% of GDP this year, almost as much as last year's, though they had promised the IMF to keep it to 3.7%. If Bolivia hopes for more outside loans, the new government will have to cut that deficit sharply. Even the relatively modest economic-simulus package that Mr Sanchez proposes—$5 billion of public works over five years—looks impossible.

Mr Sanchez thus risks suffering a plunge into deep unpopularity and rising unrest, like that being suffered by President Alejandro Toledo in next-door Peru. Trouble will come not just from Mr Morales's *cocalero* movement but from the Pachakuti Indigenous Movement, which claims to represent the Aymara and Quechua Indians who make up most of Bolivia's population. The group's leader, Felipe Quispe, peddles a colourful but historically dubious Inca revivalism, promising to free his people from the white Hispanic minority who rule them.

Behind the candidates' generous spending promises was the assumption that Bolivia's huge but mainly untapped gas reserves will provide the means. Bolivia is already selling some gas through a pipeline to Brazil, but it now wants to build another to the Pacific coast, where the gas would be liquefied and sold to America. The outgoing president, Jorge Quiroga, plans shortly to sign a treaty with Chile, to pave the way for a pipeline to its northern coastline. But this coastline used to be Bolivia's until Chile grabbed it in a 19th-century war, so nationalistic Bolivians are demanding that the gas be sent via Peru instead, which is unlikely to be economic.

Hence more impossible expectations for the new president to cope with. And even if he persuades his countrymen to swallow their pride and build the pipeline through “their” lost territory, it will be some years before the gas, and the income from it, are flowing. The gas lies under Bolivia's fertile eastern lowlands, and the wealth it will generate may increase the gap between that region and the high, chilly Altiplano where the Aymara and Quechua scratch a living. Mr Sanchez and his aides are blithely confident of being able quickly to kick-start the economy and thus defuse the tensions that have built up in recent years. With the rest of South America in a deepening crisis, this may be too optimistic.

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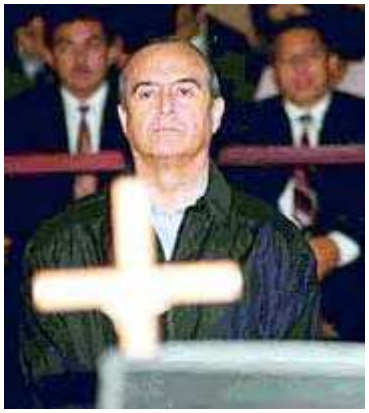
**Montesinos on trial**

# One down, just 70 or so to go

Jul 4th 2002 | LIMA
From The Economist print edition

### A first rap for the old spymaster

AP



**In his element**

STANDING stock-still, Peru's former spy chief, Vladimiro Montesinos, at last received his first prison sentence on July 1st. He got nine years for “usurping authority”: running the intelligence service and its special funds from 1991 to 2000, though this was not officially his job.

Mr Montesinos still faces more than 70 other charges arising from a corruption scandal, featuring everything from arms- and drugs-trafficking to death-squad killings, that engulfed a former government. The president then in charge, Alberto Fujimori, fled the country for Tokyo and the shelter of Japanese citizenship; Mr Montesinos fled too, but was captured in Venezuela a year ago.

Ever since, Mr Montesinos has toyed with investigators. He has refused to talk to many prosecutors and judges, but has been voluble in filmed meetings with investigating congressional committees, implicating many of Peru's top judges, politicians, army chiefs and business leaders. He is thought to have explosive information on many more public figures, and his accusations are eagerly reported.

The law is also his element, of course. Before he became Mr Fujimori's supreme fixer, Mr Montesinos was adept at “disappearing” evidence and leaning on judges. His first sentencing was delayed three times when he sacked his lawyers, then filed for removal of the judge and finally insisted that the statute of limitations had run out on the charge.

There have also been signs that the investigations are losing steam. In January the attorney-general, Nelly Calderon, replaced three of six special anti-corruption prosecutors, breaking the flow of investigations. Then a newspaper denounced her for privately meeting three generals who were under investigation by her office. It was a set-up, she insists.

Apart from Mr Montesinos, only two people have been sentenced and only one, a former congressman, Alberto Kouri, has been jailed: six years for receiving a bribe. Some feel the prosecution service has been dragging its feet. Yet the case is labyrinthine. In all, 1,310 people in 249 cases are being investigated by prosecutors, courts or Congress. Of these, 81 are in jail, 47 are under house arrest and 105 face arrest warrants but are on the run. Prosecutors say they are making progress in recovering funds stowed away in Switzerland, and have repatriated some of them.

Most of the charges Mr Montesinos faces carry sentences of, at most, 15 years, and under Peru's system they would run concurrently. So the chances of the spy chief spending longer in jail hinge on progress in human-rights and drugs-trafficking cases, which carry sentences of 25 years or more. Charges have been lodged in three human-rights cases: for a death-squad attack on a party in Barrios Altos; for ordering intelligence agents to execute leftist rebels who were captured alive after the siege of the Japanese embassy in 1997; and for engineering a fire, in which six people died, during an opposition march.

As for ex-President Fujimori, he seems safely ensconced in Japan. He faces four charges so far, including ordering death-squad killings, but Japan does not extradite its citizens. Investigators have failed to detect the funds they believe he has squirreled away, probably in Asian banks.

However, Jorge Santistevan, a former ombudsman, says Peru's efforts should not be underestimated. “The great success to date is that Montesinos and many of his associates are behind bars,” he says. The

hardest part, as he admits, is to get such people punished at all.

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Argentina

# Duhalde heads for the door

Jul 4th 2002
From The Economist print edition

**Argentina's president will step down early next year—if he lasts that long**

Get article background

HOPING to relieve the growing popular pressure for him to resign after failing to lead the country out of its deep economic depression, Argentina's President Eduardo Duhalde announced on July 2nd that he would bring forward next year's elections by six months, to March. Demands for him to go have intensified since a violent clash between protesters and police on the outskirts of Buenos Aires late last month, in which two demonstrators were shot dead. For many who have lost their livelihoods in the crash, a promise to leave early is not enough: the next day, thousands of unemployed marched on the presidential palace, the Casa Rosada, protesting at the deaths and demanding that Mr Duhalde go now.

The president insisted he alone had decided to bring forward the elections; his officials denied suggestions that the IMF and the American government had demanded this as a condition for bailing out Argentina. But the day before his announcement, the Fund's managing director, Horst Köhler, had remarked that Argentines' lack of support for Mr Duhalde's government was the country's “most difficult problem”.

Argentina defaulted on its $155 billion debts in December, shortly after violent protests brought down the then president, Fernando de la Rua. Its currency, previously pegged to the dollar, has crashed to around a quarter of its old value. With the economy in free fall, the banking system in collapse and millions of Argentines thrown into poverty, the government has been pleading with the IMF for help. But, mindful of a trail of broken promises by recent Argentine governments, the Fund refuses to budge until its long list of preconditions is met.

Argentina has in fact met most of these demands, such as getting the free-spending provinces to cut their deficits and to stop printing their own quasi-currencies. But to the exasperation of Mr Duhalde and his economy minister, Roberto Lavagna, each time Argentina fulfils a condition the IMF seems to add another to its list.

Still, in recent days there have been some hopeful signs. Mr Lavagna has persuaded the Fund to let him delay a near- $1 billion repayment due this month, which would have further depleted Argentina's dwindling reserves. And the IMF said this week that its talks with Argentina had gained a “new momentum”.

Steering Argentina through its continuing chaos is a thankless task, but several of Mr Duhalde's fellow Peronists are keen to grab the wheel. In pole position is a former Formula 1 driver, now a provincial governor, Carlos Reutemann. But revving up behind him is ex-President Carlos Menem (1989-99) who is convinced his countrymen will forgive all the scandals and the debts he ran up when he governed them. So desperate are Argentines for a return to the good old days, they just might.

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Cuba's economy

# The disaster is now “irrevocable”

Jul 4th 2002 | HAVANA
From The Economist print edition

**A non-working system is enshrined forever**

ONE more European firm suspended operations in Cuba recently. The company, a building firm working in partnership with the Cuban government, found that its partner was dipping into company funds and that workers were selling materials on the black market. Another European company wants to be available to serve its customers 24 hours a day, seven days a week; but company cars, easily identifiable by their licence plates, may be used only at certain times. *No es facil*, as people say all the time in Cuba. It's not easy for foreigners to do business here.

Cuba, out of necessity, has allowed capitalism into its socialist system. But it then keeps capitalism down, as it feels it must, with a mass of complex and sometimes contradictory rules and regulations. Just when foreigners find out how things work, the rules change again.

There are rewards, of course: most obviously, a firm foothold in a market just 90 miles (145km) from the United States, which Americans are forbidden to enter. But they barely outweigh the frustrations, and foreign investors are growing impatient. Now the European Union has presented a document to the Cuban government, laying out investors' complaints and suggesting improvements.

Government decrees, the report says, are being applied in an arbitrary and haphazard way. Bank and customs charges are prohibitively high. Cuba's comparative advantages are being eroded “by excessive overheads and by unnecessary difficulties.”“There are times when the Cubans seem to go out of their way to create obstacles,” said one European businessman with several years' experience in Cuba. “They need us, we can do business here, so I don't understand what the problem is.”

The Cuban ministry for foreign investment has held a series of meetings with European businessmen to try to iron things out. But the minister, Marta Lomas, made it clear that Cuba was not about to change its spots. “You know the rules when you get here,” she told her audience. President Fidel Castro, too, has always made it clear that he will not let such paltry matters as economic growth dilute the purity of his revolution. No dabbling with the IMF or the World Bank for him.

Meanwhile, the economy lurches on. Few people know the true figures for how bad things are, and those who do aren't telling; but tourism, the island's main foreign-currency earner, is down, and the sugar industry, its largest employer, is facing continuously low prices. Almost half the country's ageing, decrepit sugar mills are to be closed down. Meanwhile, peso shops are empty of goods, while essential items are increasingly being removed from ration books and sold for dollars only.

If the government is worried, it is not admitting it. Mr Castro's latest piece of showmanship has been to shut down factories, banks, schools and offices for three days so that Cubans could watch on television a special session of the National Assembly. The assembly was passing an amendment to the constitution to make Cuba's socialist system “irrevocable”.

In the run-up to the session, more than 8m voters—99.7% of all those registered—signed a petition supporting the measure. In hospitals, the dying were helped to sign. A few days earlier, 9m of the country's 11m people (by government estimates) took to the streets and fields in a mass rally. To celebrate, Mr Castro spoke, for several hours, about his achievements and the evils of capitalism in general. Somewhere, that EU petition gently gathers dust.

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# Brazil's football scandals forgotten

Jul 4th 2002
From The Economist print edition

Get article background

AP

Brazil's financial crisis, its plunging currency, its unemployment, poverty, violence and corruption were all forgotten on June 30th, when the national football side beat Germany 2-0 to lift the World Cup for an unprecedented fifth time. Also forgotten were the scandals that have dogged Brazilian football in recent years, and the impulse to investigate them. As the victorious players headed home, Ricardo Teixeira, the president of the Brazilian Football Confederation and one of the men accused in the congressional inquiries, repeated a promise to step down next year. But his allies hope the fans will forgive all and let him stay.

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India

# The irresistible rise of L.K. Advani

Jul 4th 2002 | DELHI
From The Economist print edition

AP

**India's leading Hindu demagogue moves a step closer to the top**

Get article background

ATAL BEHARI VAJPAYEE, India's prime minister, this week performed his most sweeping ministerial reshuffle since coming to power four years ago, swapping the foreign-affairs and finance portfolios of Jaswant Singh and Yashwant Sinha, and strengthening the leadership of his Bharatiya Janata Party (BJP). But it is another appointment that could have longer-term political significance for India, not to mention for Pakistan and the wider world. The elevation of L.K. Advani (pictured left, with Mr Vajpayee), the home minister and Mr Vajpayee's long-time political comrade and rival, to the additional post of deputy prime minister is a milestone.

Mr Advani's promotion and the lack of dissent from the ruling coalition appears to mean that the coalition's members have accepted him as the prime ministerial heir to Mr Vajpayee, who is 77 and has visibly aged in the past couple of years. This is a coup of sorts for Mr Advani, who is universally seen as the government's leading Hindu-nationalist hardliner, a reputation he first earned ten years ago when he led a movement that demolished an ancient mosque on a disputed religious site in Ayodhya, sparking widespread riots.

Although Mr Advani has since said that he regrets the demolition, there is little doubt that if the government were not constrained by its coalition partners, he would have wanted it to implement the BJP's *Hindutva* (“Hinduness”) agenda. This would include rebuilding a Hindu temple at Ayodhya and reversing laws that favour India's 12% Muslim minority. A few weeks back, Mr Advani caused alarm by threatening Pakistan with dismemberment, as in 1971. And he has several times clashed with Mr Vajpayee recently, with Mr Advani generally on the side of intransigence towards Pakistan and India's Muslims.

The nervous will see this week's appointment as a sign that the government is swinging to the right and that the BJP will not in future be prepared to see its hawkish Hindu nationalism tempered by political allies. Optimists argue that, for the time being at least, things will not work out like that. Mr Advani is ambitious. He has been softening his hardline image and trying to play down his rivalry with Mr Vajpayee. This week, at his boss's request, he persuaded Narendra Modi, the BJP ideologue who is chief minister of Gujarat, where 2,000 people died in Hindu-Muslim riots in April, to postpone a controversial

*yatra*, or tour of the state, that would almost certainly have exacerbated already deeply worrying religious tensions.

No one believes that Mr Advani—seen in the BJP as Mr Vajpayee's undisputed successor as party leader—has really tempered his nationalist fervour. But he has been careful to make himself appear more acceptable to the BJP's coalition allies. They must reckon that he is here to stay. Although only three years younger than Mr Vajpayee, he has led a more ascetic life, giving him a leaner and sharper look. By contrast, Mr Vajpayee is not expected to remain in active politics much beyond the next general election, due by mid- to late 2004—if he lasts that long.

Mr Vajpayee's administration has anyway been in urgent need of a facelift. Its defeats in elections and its failure to quell the Gujarat riots have helped the opposition Congress Party to look nationally credible again after six years in the doldrums. As well as promoting Mr Advani, this week's cabinet reshuffle is intended to reverse that trend in elections over the next 18 months in Delhi, Madhya Pradesh and Rajasthan, as well as in troubled Gujarat.

The Singh-Sinha job swap is, at first glance, puzzling. Both men have had their posts since 1998, when the coalition first came to power. Mr Sinha needed to be moved because he had failed to win much support for reform. This forced him to water down some of the main proposals in his five annual budgets, and he was blamed for adding to the BJP's unpopularity this year when tax increases hit the middle classes. Though presiding over some serious financial-market liberalisation, including opening up the insurance sector, he has failed to tackle the growing fiscal deficit and a stream of market scams.

By contrast, Mr Singh has been acclaimed as one of India's most effective foreign ministers, maintaining a strong stand through India's peace bids and crises with Pakistan, and transforming relations with America, where he became popular with senior officials in both the Clinton and Bush administrations.

Mr Sinha's logical replacement would have been one of the government's younger members, probably Arun Shourie, who has been a successful privatisation minister. But Mr Shourie was regarded as too insensitive a reformer. Mr Singh, Mr Vajpayee's first choice for finance in 1998, emerged as a logical fall-back. It then made sense to replace him with Mr Sinha.

This compromise may yet work out reasonably well for Mr Vajpayee. He now has a staunch ally in charge of the finance ministry. He can also call the shots on foreign policy through Brajesh Mishra, his national security adviser. But all this supposes that the fast-rising Mr Advani is content for the present to be a co-operative deputy prime minister, holding his instincts in check and refraining from encouraging the hardline Hindu nationalists behind the scenes. That is probably going to be the tricky bit.

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Pakistan

# Constitutional quagmire

Jul 4th 2002 | LAHORE
From The Economist print edition

**General Musharraf's plans for Pakistan are leading him deeper into trouble**

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EPA

All together now

HOW do you safeguard democracy in Pakistan? By enshrining the army in politics. Or so contends General Pervez Musharraf. In the last ten days, the president has proposed sweeping constitutional amendments which, if accepted, would transform Pakistan's Westminster-style prime-ministerial system into a presidential one in all but name, and empower him to lord it over the country for many years to come.

Among the powers the general covets are the right to appoint anyone from parliament as prime minister regardless of whether he or she commands a majority at the time; the right to fire the prime minister and/or the cabinet and parliament; the right to nominate provincial governors with powers similar to the president's in relation to the elected chief ministers and provincial parliaments; and the chairmanship of a ten-man National Security Council comprising himself and the prime minister, the four provincial chief ministers, the three service chiefs and the chairman of the Joint Chiefs of Staff.

Meanwhile, steps are being taken to ensure that general elections scheduled for early October yield a pliant, pro-Musharraf parliament, which will nod through all these amendments with the requisite two-thirds majority. A series of new laws promulgated this week should help here.

For example, politicians who have been convicted on any count from bank-loan default to terrorism are barred from standing, even if such convictions have been handed down by special “accountability” or anti-terrorist courts in their absence. This is aimed at the three most popular party leaders; ex-prime ministers Benazir Bhutto (of the Pakistan People's Party, or PPP) and Nawaz Sharif (Muslim League), and Mr Altaf Hussain, who heads the Muttahida Qaumi Movement, which has an electoral lock on Karachi and other urban areas of Sindh. These leaders also fall foul of another law requiring their parties to hold internal elections within two months—disqualifying any “convicts”.

Meanwhile, efforts are under way to use the intelligence agencies to “persuade” electable candidates to leave these parties and join the general's camp. Some say the government is hoping to provoke the main parties into boycotting the polls so that it can then hold “non-party” elections and help its own candidates win.

The opposition is not taking this lying down. Ms Bhutto is threatening to return from exile in Dubai next month and act as a focus for opposition. The Alliance for the Restoration of Democracy, which includes all the main opposition parties, is gearing up to stage rallies. Petitions are being filed almost every day before the courts challenging the proposed constitutional amendments and the new laws. The Supreme Court ruled in 1999 that General Musharraf could amend the constitution only in order to govern until the elections but could not change its basic structure. That is why he so desperately needs a friendly parliament.

If it looks as though General Musharraf cannot achieve one, some analysts believe he might postpone the elections rather than live with a hostile chamber. Yet even if he does get his way, there is no assurance his system will be sustainable. Pakistanis note the growing similarities between General Musharraf's plans and General Zia ul Haq's of almost 20 years ago. General Zia attempted a similar constitutional upheaval

in 1985, held elections which were boycotted by the PPP, and nominated a compliant prime minister. Three years later, however, the system broke down when the supposedly loyal parliament and prime minister turned against him, and he responded with absolute rule. Is this what lies in store for Pakistan?

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Afghanistan

# Taking lives, losing friends

Jul 4th 2002
From The Economist print edition

**By mistakenly killing Afghan civilians, America has harmed its cause**

ON JULY 1st, in the southern province of Oruzgan, an Afghan wedding celebration turned into a funeral. While conducting an operation against Taliban and al-Qaeda remnants, American forces, according to the Afghan government, killed at least 40 civilians and injured another 100, including many women and children. In one of the four villages said to have been hit during the operation, guests at a wedding party were killed.

What exactly happened remains unclear. The wedding victims appear to have been shot by heavy cannon fire from one of the coalition aircraft. Afghan officials have said that guests were firing into the air—an Afghan tradition at weddings—which was misinterpreted as enemy fire. According to American spokesmen, however, the pilots felt they were being targeted by sustained anti-aircraft fire and that senior Taliban were sheltering in the village.

During a two-day operation in the area, coalition planes had reportedly attacked what appears to have been legitimate targets, including an anti-aircraft gun, and a total of seven 2,000lb bombs were dropped in a cave and tunnel complex. One bomb did go astray, but it seems to have landed on an unpopulated area. Afghan officials and American military personnel have flown to Oruzgan to investigate. In the meantime, the UN is organising relief, and some of the injured children have been transferred to a coalition airbase for treatment.

While supporting efforts to root out what may be left of al-Qaeda in Afghanistan, the Afghan government has strongly criticised what it perceives as carelessness from the American-led coalition. President Hamid Karzai called on American-led forces to apply themselves more earnestly to avoiding civilian casualties and to check intelligence reports more carefully before taking offensive action. Abdullah Abdullah, the foreign minister, says there is no reason why Afghan civilians should suffer as a result of the campaign against al-Qaeda.

This is by no means the first American mistake since the war's end in which innocent Afghan civilians have died. About twenty Afghan civilians were killed during a special forces raid in January, also in Oruzgan province. And in April an American aircraft killed four Canadian soldiers.

Donald Rumsfeld, the American defence secretary, calls mistakes of this kind unavoidable. “There cannot be the use of that kind of firepower and not have mistakes, and errant weapons exist. It's going to happen. It always has and I'm afraid it always will.” But this is a high price for Afghans to pay while the coalition is having only limited success against al-Qaeda fighters, most of whom are believed to have crossed into Pakistan. So far, coalition troops have had little to show for their efforts besides uncovering weapon caches. Accidents such as this week's can only be good news for those determined to drive foreign troops out of Afghanistan.

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North Korea, South Korea and America

# The dead are not the only casualties

Jul 4th 2002
From The Economist print edition

**After yet another naval clash, talks are off, again**

Get article background

AT LEAST four South Korean sailors dead and 19 injured, and a frigate sunk by North Korean gunfire; some 30 North Koreans killed or injured by South Korea's return fire. These are not the only casualties of the clash on June 29th, the worst in three years, between North and South Korean naval vessels in the Yellow Sea, off the peninsula's west coast.

Mounting public anger this week at North Korea's latest military provocation led the South's president, Kim Dae Jung, usually bent on engagement with the North, to demand an apology in unusually strong terms. The defence minister wants a stiffening of the rules of engagement, to allow South Korean ships to open fire first at intruding North Korean vessels that ignore their warning shots. Plans to ship large quantities of surplus rice to the North have been put on hold, and new business contacts postponed. And on July 2nd, America announced that it would not send a senior official to visit Pyongyang next week, as had been planned.

The visit by James Kelly, an assistant secretary of state, was to have restarted talks between the United States and North Korea that had been suspended ever since the Bush administration took office early last year. Might this new opening have been the intended target of the Yellow Sea incident? If so, it would not be the first time that hardliners in North Korea's armed forces had torpedoed the diplomats. America's decision to send the more senior Mr Kelly, rather than the administration's usual point man on North Korea, Jack Pritchard, was a signal to the North that it wants real results.

But that may be part of the problem. America's agenda for such talks includes a halt to North Korea's missile sales; the need for North Korea to demonstrate full compliance with a 1994 agreement that offers it two western-designed nuclear-power reactors and fuel oil in return for a verifiable end to its plutonium production and a return to full compliance with the Nuclear Non-Proliferation Treaty; discussion of confidence-building measures to reduce the risk of military conflict; and better ways to monitor food aid donated through the UN's World Food Programme to alleviate hunger in the North. All are super-sensitive issues in prickly North Korea. But if the Yellow Sea clash was a deliberate effort by hardliners to scupper new talks, they have allies of a sort in Washington.

Debate smoulders there over how hard to press North Korea and how quickly, once talks resume. Earlier this year, the administration refused to certify that North Korea was in full compliance with the 1994 nuclear agreement, but then issued a waiver to allow oil deliveries to continue. That was another sort of warning shot, say some hardline officials: that unless North Korea lets international inspectors in soon to check on its past plutonium dabbling, the whole agreement will unravel. The inspectors will need at least three years to complete this work, they point out. Since this must be done before the nuclear components of the new reactors can be delivered, and since delivery is scheduled for 2005, the checks must begin now.

Others demur: if North Korea wants to put off inspections until the last minute, the project will indeed be delayed further and put in some doubt. But why look for an unnecessarily early crisis when there is a chance to open discussions with North Korea on America's full agenda?

The hawks remain unconvinced. Actual construction work on the reactors is due to start next month. The first of several hundred North Korean engineers who are due to be trained to operate them arrived recently in South Korea. But why transfer nuclear knowledge to a country that has more than earned its place in President George Bush's axis of evil, ask critics. North Korea's latest naval spat is unlikely to

have improved its evil reputation.

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China's Three Gorges' project

# Dam shame

Jul 4th 2002 | FENGJIE COUNTY
From The Economist print edition

**What happens to the villagers who dare to protest**

EPA

**The gathering flood**

IN THE village of Yaowan on the northern bank of the Yangtze River, some residents are dreading the imminent arrival of the demolition teams that will flatten their settlement and force its occupants to move elsewhere. Yaowan is one of hundreds of villages and dozens of towns that will be flooded after the world's biggest hydroelectric dam blocks the Yangtze at the bottom of the scenic Three Gorges in June next year. Many in the reservoir area, 600km (375 miles) long, complain that the government's resettlement programme is unfair and plagued by corruption. Yaowan's citizens are particularly angry.

In late May, hundreds of Yaowan's inhabitants gathered to protest against what they say is the government's failure to compensate them adequately for the loss of their land and houses. They blocked traffic attempting to pass through the village, which lies on a main road running through Fengjie County at the entrance to the gorges. Elderly villagers sat on rocks placed in the middle of the road, until the authorities lost patience.

The government is fearful of unrest that could cast more doubt over the controversial project and complicate the task of relocating more than 1.2m people, or perhaps as many as 2m according to some Chinese experts. Criticism of the project is rarely allowed to appear in China's state-controlled media. But in 1999 a Chinese academic wrote in a leading journal that the resettlement of reservoir-area inhabitants could become “an explosive social problem, a source of constant social instability in our country for the first half of the next century.”

It already is a huge social problem. A scarcity of arable land means many of those resettled will have to move far from their homes. The finance ministry has recommended relocating them to sparsely populated areas such as Tibet and Xinjiang, which will fuel anti-Chinese sentiment among ethnic minorities in those areas. Compensation payments are woefully inadequate and much of the little that is available is drained away by corruption. The government admitted two years ago that some $58m of resettlement money, out of $2.1 billion then allocated, had been misappropriated.

But the government does not want evacuees airing their grievances in public. Early last year, the authorities arrested four farmers in Yunyang, in the next county upriver from Fengjie, who had complained to foreign journalists about corruption among officials in charge of resettlement. The farmers were accused of leaking state secrets.

In Yaowan village, hundreds of police and paramilitary troops were deployed to stop the protests. Participants say the protests were peaceful. Officials say some villagers violently resisted attempts to disperse them. The police detained more than a dozen people, of whom villagers say nine remain in custody. They say the police are still looking for organisers. “We don't dare to speak out,” says one villager. “If we do, we'll be arrested.”

Protests such as those in Yaowan could become more frequent in the coming months as the resettlement process moves into high gear. Between the start of the Three Gorges dam construction in 1993 and the end of last year, 458,000 people were moved. This year alone, another 148,000 will have to relocate. The aim is to complete the process by the end of the year, including the demolition of buildings beneath the reservoir's initial water level. But even though demolition teams have already reduced much of the riparian settlement between the dam site and Chongqing, at the head of the reservoir-to-be, there is much work to be done.

The government tried to create a sense of urgency in January by organising television coverage of the dynamiting of Fengjie County's government headquarters in Yongan and a disused power station. But much of Yongan is still standing. Its narrow streets, known as a haunt of some the nation's most famous classical poets, still teem with life. Its decades-old rubbish tips have yet to be moved, if they ever will be. A Chinese newspaper said in a forthright report in February that the reservoir, filled with refuse, could breed disease.

Much of the new county seat, high above the river, is still a building site, though government and Communist Party organs have already occupied their lavish new offices and a few senior officials have moved into luxury five-bedroom apartments overlooking the river—suspiciously comfortable given that Fengjie is relatively poor. Most of Fengjie's urban residents will end up with better housing. But the compensation scheme provides free housing only up to the same size as residents' cramped homes. Since most of the new accommodation is bigger, residents have to pay premium prices for the additional floor space. “Ordinary people have to spend a lifetime's savings for a new place,” says the manager of a Fengjie removal company.

But the dam-builders are not holding back. On July 1st, the Chinese Communist Party's 81st birthday, the last coffer-dam protecting the dam itself from the full might of the Yangtze river was blown up, two months ahead of schedule. One of the dam's most vocal critics, Dai Qing, who once worked on a leading state newspaper, says that in spite of the project's many drawbacks, many officials see it as a way of lining their pockets. She laments that some former officials have already acquired enough money to move abroad, leaving the dam and its problems for others to deal with.

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A report from Congo

# Africa's great war

Jul 4th 2002 | BUKAVU, KINSHASA AND KISANGANI
From The Economist print edition

Sven Torfinn

**Congo's civil war may have claimed as many as 3m lives. The country is so inaccessible that its horrors are rarely reported**

Get article background

IN THE chocolate waters of the Congo river, a mutilated corpse rolls by. The rebels' "minister for children" shivers. How is he going to explain this to the horrified UN peace envoys from the capital, Kinshasa, who are at that moment stepping on to the quay to meet him? Not by telling the truth, obviously, which was that his rebel group had slaughtered 150 people in the town of Kisangani on May 14th-15th, then pitched their disembowelled bodies into the river with stones crammed into their bellies. Instead, he smiles, accepts the envoys' offerings of food aid, and talks chummily of other things.

Over the past four years, Congo's war has claimed more lives than any other. The International Rescue Committee, an American aid agency, says that by the middle of last year, 2.5m people had died because of the war in eastern Congo alone. Some were shot or hacked to death; many more succumbed to starvation or disease as nine national armies and a shifting throng of rebel groups pillaged their country. By now, the death toll is probably over 3m, although this is the roughest of estimates. As one UN worker puts it: "Congo is so green, you don't even see the graves."

Western powers seem barely to have noticed the catastrophe. This is partly because, unlike the Middle East, Congo has no strategic importance. But it is also because it is two-thirds the size of Western Europe, thickly-forested, incredibly dangerous and has hardly any paved roads or working telephones. Simply finding out what is happening in Congo is a challenge, as your correspondent discovered while accompanying militiamen on patrol by the shore of Lake Kivu last week, when he was forced to hide in a bush to avoid 200 hostile Rwandan soldiers passing by.

And yet there is hope. In April, the Congolese government signed a peace deal with most rebel groups. By offering rebel leaders a share of power, the government won nominal control of 70% of the country (see map below). This part of Congo is now relatively peaceful, and slowly recovering economically. But one important rebel group refused to sign. The Rwandan-controlled Rally for Congolese Democracy (RCD), whose minister for children brazened out the watery corpse, still holds most of eastern Congo.

Here, the war blazes on. Or rather, dozens of overlapping micro-wars flicker, in which almost all the victims are civilians. A typical village can expect to be looted by several different bands of armed men. Under what amounts to Rwandan occupation, eastern Congo is arguably the most miserable place on earth.

**Room for improvement**
Democratic Republic of Congo, 2000

| | |
|---|---|
| GDP per person, $ | 90 |
| Population per doctor | 24,319 |
| Telephone lines per 1,000 people | <1 |
| Life expectancy at birth, years* | 51 |
| Access to safe water, % | 45 |
| Undernourishment, %† | 61 |

Sources: UNDP; World Bank; Oxfam *1999 †1998

## A rough neighbourhood

The story of Congo's war began in 1994, with the genocide in Rwanda, Congo's tiny neighbour. A government dominated by Rwanda's Hutu tribe tried to exterminate the Tutsis, a prosperous minority. In 100 days, 800,000 Tutsis, and Hutus who refused to co-operate, were murdered. The slaughter stopped when an army of exiled Tutsis invaded from Uganda, and drove the killers into Congo (which was then called Zaire). The new, Tutsi-dominated government in Rwanda was afraid that the *genocidaires* would regroup and return to finish the job. So when Mobutu Sese Seko, Zaire's dictator, gave them succour, Rwanda engineered a rebellion that toppled him.

In his place, the Rwandans installed a guerrilla leader and drunk, Laurent Kabila. They hoped he would do their bidding. Instead, he rearmed the *genocidaires*. So Rwanda tried to topple him, too. With help from Uganda and Burundi, it nearly succeeded. Kabila was saved by five friendly nations, of which the most effective were Angola and Zimbabwe. Most of the countries that intervened had legitimate interests in Congo. Rebels from most neighbouring states were using Congo's lawless forests as a base from which to launch cross-border raids. The failure of the Kabila government to curb these rebels prompted Rwanda, Uganda and Angola to enter the war. Zimbabwe, which shares no border with Congo, sent troops for different reasons: to satisfy the power-broking pretensions of its president, Robert Mugabe, and his army's appetite for loot.

Before long, the war reached a stalemate and the miscellany of armies settled down to the serious business of plunder. Zimbabwe bagged diamond seams in the south. Angola joined the Congolese government in an oil venture. Rwanda and Uganda began digging for diamonds and coltan (a mineral used in mobile telephones), harvested timber and ivory, and even emptied schools of desks and chairs. Though supposedly allies, Rwandan and Ugandan troops have occasionally clashed over the spoils. But in general, the more all the armies plundered, the less willing they became to fight each other (as opposed to unarmed peasants).

## A younger, thinner, nicer Kabila

Then, in January last year, one of Kabila's bodyguards shot him once in the gullet and twice in the guts. No one knows who gave the order, because the assassin was himself killed almost immediately. One rumour is that his allies were so sick of his double-crossing that they had him killed.

Kabila's legacy is not a happy one. At his mausoleum in Kinshasa, a bronze statue shows the dead president clutching a book, which is an odd memorial for a man who halted book-keeping at the Congolese finance ministry. In the parts of Congo he controlled, Kabila ruled as despotically as his predecessor, but less competently. He scared off investors by jailing foreign businessmen and demanding million-dollar ransoms. He banished aid by insulting foreign diplomats. By printing money while enforcing price controls, he caused Soviet-style shortages. By the end, petrol was so scarce that the state oil firm resorted to flushing its main pipeline with river water to force out the dregs.

Kabila was succeeded by his son, Joseph. Now 31, Mr Kabila junior is doing a better job. He endorsed a peace plan that his father rejected. A ceasefire followed, policed, where possible, by the UN. Angola withdrew to its border, and Uganda pulled out some troops, leaving others to mind its businesses in northern Congo.

Zimbabwe stayed, at the government's request. The young Mr Kabila wants to be protected from the Rwandans, who refuse to leave. The Rwandan government says it will not withdraw its army, which occupies a slice of Congo 27 times bigger than its own country, until the last Hutu fighter has been

captured or killed.

Rwanda reckons that 55,000 Hutus, still intent on genocide, continue to lurk in Congo's jungles or have joined the Congolese army under false names. The estimate of the International Crisis Group, a think-tank, is half that number. All the same, to prevent the Hutus from regrouping and invading Rwanda, the UN has proposed setting up a Congo-based border force. Mr Kabila's government accepts this. To show goodwill, it has already released 2,000 Rwandan Hutus from its army and invited the international genocide tribunal to investigate. But Rwanda says no.

No one is suggesting that Rwanda's fears are unfounded. Yet many observers say that Rwanda and its pet rebels are no longer pursuing the *genocidaires* with much passion. Refugees from Mwenga, a bush-town in South Kivu, a mineral-rich province, complain that their homes were attacked by Hutu militiamen a dozen times in the past two months, but that the town's Rwandan garrison did nothing. The townspeople say they asked the Rwandan commander why. He is said to have replied: “These are our brothers, do you think we can kill them?”

Another example: the Hutus' camps on South Kivu's Ruzizi plain are well known to the Rwandan troops nearby, say UN officials, but they are seldom, if ever, attacked. A local Hutu commander claims that the Rwandans regularly supply him with arms. Elsewhere, according to a senior Rwandan officer who recently sought asylum in Belgium, the army hires Hutu militiamen to work its coltan mines. He told the Belgian senate that they could otherwise be eradicated “in less than a month”.

Besides securing its own borders, Rwanda claims to be protecting Congo's ethnic Tutsis, the foot-soldiers of its two rebellions, from being murdered by Hutu militias or other Congolese. But even this group is now rising against Rwanda's occupation. Early this year, a brigade of Congolese Tutsis mutinied and returned to their tribal homeland, in the hills above Lake Tanganyika. Around 1,000 rebel fighters have deserted to join them. Rwanda swiftly sent 8,000 troops to crush the revolt, and is now reportedly herding Tutsi villagers into a barren camp, to stop them feeding the deserters. Tutsi against Tutsi, this is now the fiercest battle of the war.

With mid-ranking rebels meanwhile crossing to the government side, and senior rebels expected to follow, the RCD could be on the verge of disintegration. Rwanda has tried to deter desertions by force, of which the massacre in Kisangani was an example. But if the RCD crumbles, Rwanda will doubtless find an alternative cover for its occupation of eastern Congo. Indeed, it has already started looking: in June, Rwanda deposed the RCD“government” of South Kivu, and replaced it with the leaders of a more pliable militia.

The players change; but the game remains the same. This is bad news for the hapless people of eastern Congo. Everywhere they look, they see men with guns. Besides the Hutu militias, the Rwandans and their rebel allies, there are the Mai-Mai, a warrior cult, and myriad gangs of bandits. All prey on the poor.

Across Kivu, a land of postcard-perfect green hills, villages are half-deserted, fields neglected and livestock a fond memory. In the forests around Mantu, near Bukavu, villagers have dug waist-deep trenches and covered them with branches. When Hutu marauders come, as they do most weeks, they hide in these holes.

The peasants of Ramba Chitanga, a village too tiny to appear on any map, tell a grisly tale. When the RCD left, Hutus moved in, and accused the villagers of feeding their enemies. Then the Mai-Mai attacked. During the ensuing battle, the Hutus hacked off 29-year-old Janet Vumilia's hands. Now, with her skittle-like stumps, she ticks off the relatives they killed: her parents-in-law, her brother-in-law, her pregnant sister, her niece.

Villagers say they can distinguish different factions by their actions. The Hutus, they say, are more vicious than the Mai-Mai, while the rebels are more likely than the Rwandans to abduct children. But sometimes the distinctions become blurred. Francine, a 14-year-old new mother, says she thinks her

baby's father was an RCD rebel. But he could have been a Mai-Mai; men from both groups raped her. When her father objected, the Mai-Mai slit his throat.

In Kivu, cattle are now scarce, yet livestock prices have plummeted. Locals calculate that if they buy a cow, armed men will take it, so they don't buy cows. The rebels levy a “security tax” of $1 per hut, but payment does not seem to reduce the likelihood that, sooner or later, killers will come in the night.

In Walungu hospital, near Bukavu, 1,200 patients compete for 300 beds, and the attention of three doctors. About half the inmates are relatively healthy, but too terrified to go home. Murals in the hospital depict black doctors in white coats peering into microscopes, recalling the lost hopes of the 1960s. Now, the wards are full of black children with blonde hair, a sign of malnutrition. The hospital's 32-year-old head of nursing says she has received only three months' salary in her whole career. Why does she carry on? “It's our country,” she shrugs. “It's painful, but there it is.”

If Rwanda had been a benevolent occupier, it might have turned a profit without stealing. As Congo's infrastructure crumbled over the past 40 years, people in the east of the country strengthened their commercial links with Rwanda. This trend accelerated when war closed the Congo river, the country's main highway, severing eastern Congo from Kinshasa. Had the Rwandans built a decent road or two linking eastern Congo with Kigali, their own capital, they could have exploited this.

Instead, they chose to murder and plunder. “We couldn't believe the things these people did during the genocide, until they came and started doing them to us,” said a market-woman in Bukavu, jumbling together Hutu killers and Tutsi invaders.

## Heroic optimism

In Kinshasa, meanwhile, stinking bank notes suggest that things are looking up. The new government printed no money in the second half of last year, and lifted price controls. Inflation is currently below 5%, down from 511% in 2000. On June 13th, the World Bank approved a $450m loan, part of a multilateral aid package that could total $1.7 billion. The Bank's new man in Kinshasa, the first posted there in a decade, says that Congo could be about to see surprisingly rapid development.

This is heroic optimism. Congo's institutions are as dirty as its bank notes. Corrupt parastatals disgorge no revenue to the central bank. Their past thieving has saddled Congo with $13 billion in debt. Civil servants make ends meet by demanding bribes or doing other jobs on the side. In the offices of the immigration ministry, for example, not only visas but also sexual favours are for sale. Respect for human rights has improved under the new regime, but only a bit. Political troublemakers, and journalists, are regularly arrested. Policemen and soldiers, often drunk, in mirrored sunglasses, freelance as muggers. During a random “visa inspection”, *The Economist*'s correspondent was bundled into a black Mercedes and relieved of $450 by four men claiming to be security officers. It could have been worse: an American aid worker was recently beaten senseless after overtaking a general on the boulevard.

Whether Joseph Kabila could control these abuses is unclear. He is popular throughout Congo, because people regard him as the best hope for peace. But he has some ugly people around him, including some of the worst crooks and thugs of his father's administration, and of Mobutu's too. The people of Congo tell anyone who asks that they want their country to be united, invader-free and democratic. The prospects for this are woeful, in the short term at least.

Mr Kabila has promised to hold free and fair elections as soon as the country is reunited. But no Congolese leader has ever kept such a promise before, and some of Mr Kabila's allies have cause to try to prevent the young president from keeping his. For example, Mwenze Kongolo, who is Mr Kabila's uncle and Mr Mugabe's good friend, is associated with the worst abuses of the old Kabila regime, and so cannot expect anyone to vote for him. He is however popular with certain army brigades.

If Congo's different factions agree about anything, it is that white foreigners are responsible for their troubles. Given a history of western meddling—King Leopold of the Belgians plundered Congo in the 19th century, and America first propped up Mobutu and then helped overthrow him—such a view is understandable. But it is hopelessly out of date. Since the cold war ended, western governments have seen no reason to care much about Congo.

Mostly, they ignore it, considering its problems too tangled to solve. The UN's ceasefire-monitoring mission consists of only 442 military observers. Efforts to disarm the militias in eastern Congo have been

crippled by the RCD's refusal to grant the UN free passage.

Since 1994, western donors have put a bigger effort into Rwanda than Congo. In part, this stems from guilt at having failed to stop the genocide. It is also because bite-sized Rwanda's problems seem more manageable, and its efficient government is refreshing to deal with. Throughout Congo's war, aid has poured into Kigali.

All the same, Rwanda's behaviour in Congo may soon cost it some friends. In August, a UN Security Council panel will deliver its third report on the looting of Congo's resources, focusing on the humanitarian impact of Rwanda's plunder in the east of the country. Sanctions, or at least a reduction of aid, are possible. Britain, Rwanda's biggest bilateral donor and keenest apologist, is expected to oppose such moves. But France will probably be in favour. And the Americans may be willing to go along with some sort of censure of Rwanda, even if it is only a reprimand.

AP

**The pity of war**

It will take more than a reprimand to eject Rwanda from Congo. Its leaders—the Tutsi fighters who stopped the genocide—have turned their country into one of the most militarised in Africa. By plundering Congo, some have found a way of enriching themselves without upsetting their own people. Meanwhile, war gives Rwanda's president, Paul Kagame, an excuse to squelch dissent and muffle the press. It also keeps at least 20,000 unruly, mostly-Hutu soldiers from coming home and stirring fresh trouble in Rwanda, where it all began.

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Turkey's government

# No place for a worn-out prime minister

Jul 4th 2002 | ANKARA
From The Economist print edition

AP

**Bulent Ecevit is sick. Turkey risks being so too, if he insists on hanging on to power**

Get article background

JUST go. That is the message from Turkish businessmen, politicians and commentators of all ideological hues to Turkey's ailing prime minister, Bulent Ecevit. But after spending nearly two months in bed under the care of his autocratic wife, Rahsan, the 77-year-old prime minister, whose afflictions range from a spinal disorder via cracked ribs and a thrombosis to loss of appetite, is clinging mulishly to power. In so doing, he is putting at risk not only a crucial economic-recovery programme being overseen by the IMF, but the very future of Turkey, a strategic pivot between Europe and the Middle East.

Mr Ecevit insists that he must remain in charge until April 2004, when parliamentary elections are next due. But his last public appearance, after a meeting with his coalition partners last week, the first in more than 40 days, dispelled any remaining hopes that he is fit to do so. Stumbling over his words, his voice quavering, Mr Ecevit was hard pressed to string together an intelligible sentence as journalists camped outside his official residence bombarded him with questions about the future of his government.

It is an awkward coalition: his own Democratic Left, the centre-right Motherland party and the far-right Nationalist Action Party. Yet until recently it has been among the more stable in Turkey's modern history. It could yet hold together, keeping reforms—and on the financial side they have been sweeping—on track. But only if it gets a new leader, and fast.

A recent fall in interest rates had inspired confidence that Turkey was coming out of its fierce recession. Mr Ecevit's ill-health has reversed these hopes, in turn unleashing fears that the country will not be able to roll over its total public debt of some $200 billion. The IMF, which has pledged Turkey loans worth $17 billion, could well wonder whether to come to the rescue again.

On the political front, the European Union is demanding a range of reforms before it will name a date for starting negotiations on Turkish membership. Mr Ecevit's ill-health has put these on hold. They include scrapping laws that criminalise free speech; allowing the use of the Kurdish language in education and broadcasting; abolition of the death penalty; and ending torture in police cells or prisons.

The government last month decided to lift the state of emergency in two mainly Kurdish provinces in the south-east, leaving only Diyarbakir and Sirnak, which is on the Iraqi border, under such rule. But parents

across Turkey are still being prosecuted for giving their children Kurdish names, and publications fined for using the letter W, part of the Kurdish alphabet but not the Turkish one, on the ground that such things encourage ethnic separatism.

An accord in Cyprus remains out of reach, which increases the risk that the EU will admit what would, in practice, be only the Greek-run bit of the island on its own—and that Turkey's own hopes of EU membership would be swamped by nationalist and Islamist sentiment. Turkey, as one EU diplomat puts it, might then go down “the Uzbek road”, becoming nothing more than “an aircraft-carrier for the Americans” from which to harry Iraq and Iran.

That need not happen. The great majority of Turks, and indeed Turkish Cypriots, want to join the EU. That may mean some arm-twisting of Rauf Denktash, the Turkish-Cypriot leader. But Mr Ecevit on his sickbed is not the man to do it.

The road ahead could be an extraordinary congress of his party and election of a new leader, who could then reasonably aim to take over as prime minister. But whoever got the job would have to be blessed by Mr Ecevit—or would be seriously weakened from the start.

Who could this be? Maybe Husamettin Ozkan, a deputy prime minister from Mr Ecevit's party, who is widely credited with bridging differences within the coalition. Or the foreign minister, Ismail Cem, a committed Europhile, well liked by the public, though less so within his own party. But the best choice, for many Turks as for western governments, would be Kemal Dervis, the economy minister, who was brought in last year from a job at the World Bank. He is hardworking, honest, personable and a firm backer of the sorts of changes sought both by the EU and the IMF. The snag is that he is not now a member of any party, let alone Mr Ecevit's.

There is another snag: Devlet Bahceli, the Nationalist leader and also deputy prime minister. His party is the second-largest in parliament, and he has hinted that he will pull out of the coalition if Mr Ecevit steps down. He has also threatened to do so if the government strikes a deal with the opposition to end the death penalty, so sparing the neck of Abdullah Ocalan, the captured Kurdish rebel leader.

That would bring down the government and probably force the president to call a general election. And then? Polls suggest that none of the parties in the ruling coalition would even get the 10% of votes needed to win seats at all (a point Mr Bahceli might well consider before pulling the plug) and that Recep Tayyip Erdogan and his Islamic-minded White party would grab the biggest share.

That would upset Turkey's American allies, who distrust his attitude to the West and to Israel. It would also upset Turkey's fiercely secular generals. Most probably they would block Mr Erdogan's road to power, and in so doing further tarnish Turkey's democratic credentials.

Unsurprisingly, therefore, the generals are thought to be quietly campaigning for Mr Ecevit to go—but not until he has named a successor. Just who they have in mind is unclear. But almost anyone who is not an Islamist, by now even Mr Bahceli, looks preferable to the uncertainty that would follow a general election.

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Italy's government

# A blow to the prime minister

Jul 4th 2002 | MILAN
From The Economist print edition

**A powerful Italian is punished for an ungracious remark**

AP

**Scowling Scajola's howler**

IT STARTED as a tragedy in Bologna in March. It ended up this week in Rome with a string of embarrassments culminating in the resignation of one of Italy's most powerful politicians, Claudio Scajola, the interior minister. And the affair is not yet over. The murder of Marco Biagi, a professor who was advising the right-wing government of Silvio Berlusconi on how to loosen up the labour laws, has turned into a messy business on many levels.

The police do not seem close to catching the killers, who call themselves Red Brigades after the terrorists who shot their way into Italian history with a wave of murders in the 1970s and early 1980s. In the past week or so, the police's shame has been increased by the publication of five letters which suggest that Mr Biagi's death could have been prevented.

They were written by Mr Biagi himself, pleading for help after receiving a series of death threats. Plainly, nobody took them seriously enough. The letters were written on the professor's own computer, which the police failed to examine when they started investigating his death. Mr Biagi begged several prominent people, including parliament's speaker and the head of Confindustria, the employers' club, to help him persuade the government to give him more security, since he feared for his life: three years ago terrorists had killed another leading reform-minded labour-ministry adviser, Massimo D'Antona.

The fallout has descended on two people in particular: Mr Scajola and Sergio Cofferati, leader of CGIL, Italy's largest trade-union group. As interior minister, Mr Scajola had the final word in giving special protection to individuals. Mr Cofferati has been the most dogged opponent of reforming Italy's rigid labour laws. Professor Biagi complained in his letters that Mr Cofferati was “criminalising” him.

Though stung by these accusations, Mr Cofferati refused to criticise the murdered professor. Mr Scajola showed less sensitivity. He called Mr Biagi a “pain in the arse” interested mainly in having his government consultancy renewed. Italians were shocked. Italy's president, Carlo Azeglio Ciampi, apologised to Mr Biagi's widow. Virtually all opposition politicians and many in Mr Scajola's own coalition demanded that he should go. And he did.

This was something of a surprise. Mr Scajola, a tough and shrewd Ligurian, was perhaps the most powerful man in government after Mr Berlusconi himself, who is still doubling up as foreign as well as prime minister. It was Mr Scajola who turned Mr Berlusconi's Forza Italia (Go, Italy!) movement into a real party, which won last year's election so handsomely. He may well have been the most influential of Mr Berlusconi's friends. Despite having mismanaged a meeting for the G8 rich countries last year in Genoa, he seemed secure in his job. But answering the sensible question as to why his ministry skimped on security for Professor Biagi with an insult was too much. Mr Berlusconi has asked another of his oldest friends, Giuseppe Pisanu, to fill the gap.

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Portugal's public finances

# Too much red ink for the euro-zone

Jul 4th 2002 | LISBON
From The Economist print edition

**Last year's deficit broke the rules. Ought this year's government to be punished?**

PORTUGAL has become the first country to plead guilty to a capital crime under the euro-zone's growth and stability pact. Answering a parliamentary question last week, the new centre-right prime minister, Jose Manuel Durao Barroso, blurted out the scale of—yes, the previous, centre-left government's offence: a budget deficit in 2001 of 3.9% of GDP, far above the pact's 3% limit, and much higher than any previous official figures. And now for the sentence of the court?

The full force of the law, says Pedro Solbes, the European commissioner for economic and monetary affairs: if the 2001 deficit is confirmed to be above 3%, the commission will not hesitate to apply the rules, so Portugal could face fines of up to 0.5% of GDP and/or be denied access to the European Union's "cohesion" funds.

Well, maybe. The threat is meant to deter, not actually to be applied. Mr Durao Barroso says it would be "incomprehensible" to punish Portugal this way, just when his coalition government is implementing painful austerity measures to cut the deficit. So why invite trouble, asked his critics, by publicising the figure of the deficit, which until he did so had been kept under wraps by the European Central Bank? The country "has a right to know", he replied.

Again, maybe. The new government, which took office in April, is indeed trying to lessen the deficit. The better "the country" knows how big a problem it faces, the readier voters may be to accept its tough measures, which have already seen Mr Durao Barroso's support fall behind the Socialist opposition in some opinion polls. And the bigger the 2001 deficit, the more credit to him if he can bring the 2002 deficit down to the proposed 2.8% of GDP, a target which Mr Solbes had earlier criticised as not being bold enough.

This is a risky strategy. The prime minister has incurred displeasure by leaking the ECB figures and pre-empting the findings of a commission, headed by the governor of Portugal's central bank, that is due to determine the definitive 2001 deficit by the end of July. He may also have pushed the European Commission into asserting its authority, at a time when more than one EU government would like to ease the obligation to reach budget balance by 2004, and when France has already been allowed a bit of leeway. Rapping little Portugal over the knuckles might be seen as a way of discouraging grander folk.

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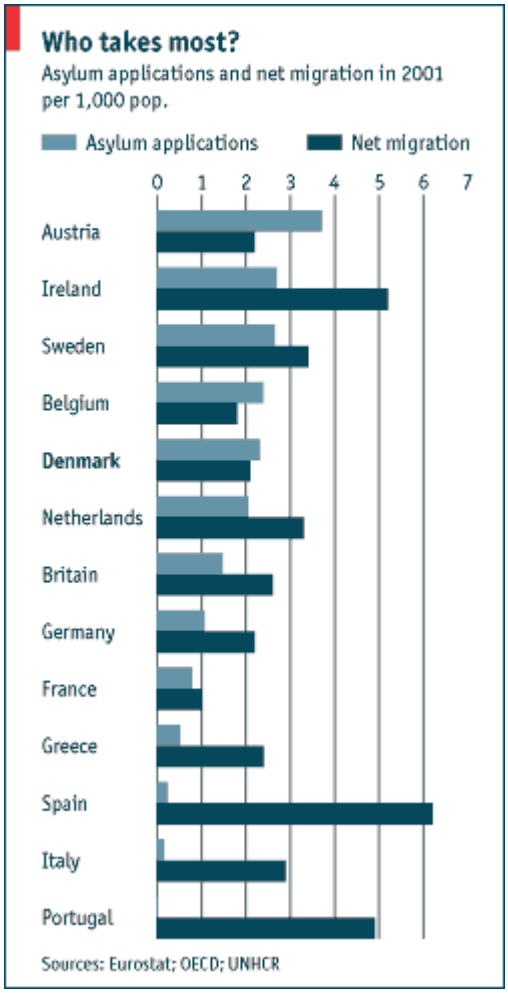
Denmark and asylum

# The welcome-mat has gone

Jul 4th 2002 | COPENHAGEN
From The Economist print edition

**And the rush of people claiming asylum has suddenly slowed**

THE Margretheholm centre for asylum-seekers, a down-at-heel former army barracks ten minutes' drive from the heart of Copenhagen, will close at the end of August. Over the past six months, the number of refugees seeking asylum in Denmark has almost halved. With fewer refugees to cope with, the Danish Red Cross is planning to close 16 of its 32 reception centres.




Refugees and administrators at the Copenhagen centre are in no doubt about what is going on. Denmark's new laws to deter asylum-seekers are having their intended effect. A young Iraqi at the centre, who has just had his application turned down, says that when he set off for Europe two years ago the word was that Denmark offered a “golden asylum”. It was high in the European Union's league of asylum-seekers per head of population.

But a lot of Danes began to balk. Asylum-seekers, they complained, were exploiting the country's generous welfare state. Immigrants, they claimed, were responsible for rising crime. The anti-immigration Danish People's Party got 12% of the vote in last November's general election. Though it has no ministerial posts, the new, right-leaning minority government of Anders Fogh Rasmussen depends on its support in parliament. Mr Rasmussen says he definitely had to “stop immigrants who take advantage of a very generous welfare state”. His government has cut back benefits for asylum-seekers and now forbids any resident of Denmark from bringing in a foreign spouse who is under 24 years of age, a move aimed against arranged marriages, which were swelling the country's immigrant population.

More important than the measures taken by the government is the general message it has sent out. Merethe Laubjerb, the Margretheholm centre's director, says that after the law was passed “things changed very quickly. People are calling their families and calling each other...people are aware that it's not comfortable to go to Denmark.” Neighbouring Sweden has now seen a sharp rise in the number of asylum-seekers turning up on its doorstep.

The People's Party is pleased. Rasmus Hjordt, its spokesman, says that Muslim immigrants have been changing Denmark for the worse, asking for girls to be excused from gym at school and for pork to be taken off schools' menus, for instance. Immigrants, he claims, are responsible for 68% of all rapes in Copenhagen—a figure contested by newcomers' support groups. He says that the government's new law met most of his party's initial demands. And he feels that the rest of Europe will soon emulate Denmark's new policy. “Holland, the United Kingdom, Italy: they're all going the same way.”

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France's new plan

# Too good to be true?

Jul 4th 2002 | PARIS
From The Economist print edition

**France's president has said most of the right things. But will he deliver?**

Get article background

JACQUES CHIRAC's message, read out on his behalf this week to both houses of the French parliament, was clear enough. “By the middle of this summer, you will have passed bills to strengthen the state's authority, guarantee the French people's safety, restore France's competitiveness and ensure the nation's solidarity.” In other words, the election celebrations are over and an extraordinary month-long session of the National Assembly and Senate must begin forthwith.

It is easy enough for a president, prevented by a constitutional separation of powers from declaiming in person, to declaim from on high; the senators and deputies stood up to listen in respectful silence, apart, that is, from three Socialist deputies who stayed seated in protest at this “monarchical” behaviour. But how exactly will the government of Jean-Pierre Raffarin, even with a pro-Chirac majority of 399 of the National Assembly's 577 seats, fulfil the president's wish-list? As a former economic adviser to Mr Chirac puts it, “Now is not a good time to be prime minister.”

Quite so. The president has promised a cut in income tax of 5% in September and a cut of up to one-third over the course of his five-year term. His promise to “strengthen the authority of the state” means tackling crime with more police and expensive new prisons. His pledge to “restore competitiveness” means lowering taxes on business, making the 35-hour working week more flexible, inviting bosses and workers to negotiate new deals on unemployment and health insurance, and slimming down the public sector—and any part of this could all too easily send the unions on to the streets in protest.

Perhaps the deceptively unassuming Mr Raffarin will prove equal to a task that in 1995-1997 was so clearly beyond the unpopular Alain Juppé, the last pro-Chirac prime minister. The day after Mr Chirac's message, Mr Raffarin faced parliament for a full 80 minutes to outline what he called his government's “programme without arrogance”. In truth, however, save for a flat rejection of European Union plans to cut France's fishing fleet, he added little to what had already been declared in the president's message or in the earlier election manifesto. Meanwhile, friends and foes alike are well aware that Mr Raffarin's margin for manoeuvre is narrow.

Mr Chirac's promises, worked out before the presidential elections of April and May by his astute economics adviser, Jean-François Cirelli, are based on an annual economic growth rate of 3%. Yet this year it will be about half that. Moreover, an audit commissioned by the new government of the nation's accounts revealed last week that the budget deficit for this year will be between 2.3% and 2.6% of GDP, compared with the 1.8% predicted (doubtless with a self-serving pre-election optimism) by the now-defeated left-wing government as recently as February. Translate that into money, and it means that the deficit may widen from the *euro*30.4 billion ($30 billion) originally inscribed in this year's budget to as much as *euro*45 billion.

Naturally, the audit is self-serving. If promises have to be broken, it will be easy enough to blame the set of books inherited from the left. Similarly, even though the new finance minister, Francis Mer, has already persuaded the European Commission to loosen the rules that say that all EU countries must balance their public budgets by 2004, he can still blame the Union if promises have to be broken.

But in the long term what will matter most is not the promises' arithmetic but the reforms that will have to accompany them. Jean-Claude Trichet, the governor of the Bank of France (and presumed next head of the European Central Bank), declared this week that social services, the labour market and education all need reform, both to improve French industry's competitiveness and to reduce government spending,

which last year was 52.6% of GDP. As Mr Trichet noted, Austria is the only other euro-zone country in which government spending accounts for more than half of economic output.

Clearly, all this is more easily advocated than achieved. How, for example, will Mr Raffarin reform a demographically unsustainable pensions system which offers earlier retirement and better benefits to the fully unionised public sector than to the less unionised private sector? And will strike-prone railway workers and others in that public sector take kindly to the idea that they should “guarantee” a minimum level of service to the public?

Yet if the president's dreams leave the prime minister with a headache, so be it. After all, it is hard to disagree with the president's declared intention to “protect the weakest, reduce unemployment, fight poverty and exclusion, and struggle resolutely against the discrimination that flouts the essence of the French ideal.” And the business community, so often ignored by the outgoing government, will be delighted by his pledge to set free the country's entrepreneurial spirit and to let the French “profit from their efforts”.

In the end, however, the most far-reaching of this presidency's proposals may turn out to be a change of administrative rather than economic policy. “The moment has come”, declared Mr Chirac, “to resume the long march, so often thwarted, towards decentralisation. I call for a great national debate on local freedoms and responsibilities.” Translate that into action (the prime minister invited the regions, including the troubled island of Corsica, to experiment as a matter of pragmatism rather than ideology), and the Raffarin government will be devolving to the regions more tax-raising powers—and the responsibilities that go with them. Since that, in turn, will mean a lessening of the powers of the Parisian elite, the debate should be interesting.

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A controversial German appointment

# Unwed mother as family guardian

Jul 4th 2002 | BERLIN
From The Economist print edition

**To win elections, conservatives must avoid looking fuddy-duddy**

AP

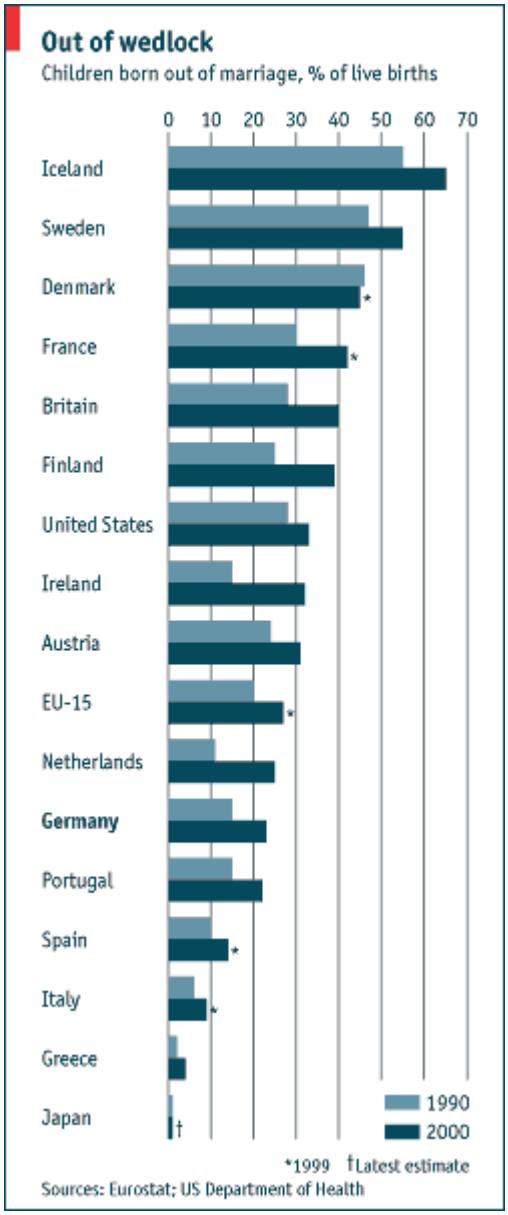
**The Reiche new lady for the right**

SHE sounded like the answer to Edmund Stoiber's prayers. Katherina Reiche is 28, clever, good-looking, hails from the former communist East Germany, and combines motherhood with a successful political career. What more could a silver-haired chancellor candidate, surrounded by a greying, predominantly male team from western Germany, want in order to jazz up his campaign and attract votes from where they are least forthcoming—from women and from *Ossis* (easterners)? Mr Stoiber pounced, this week announcing her appointment as the fifth member of his "team of experts", a kind of shadow cabinet, and making her responsible for policy on women, the young and the family.

But instead of joy there is embarrassment and gnashing teeth. For Ms Reiche, who already has one child and is expecting another next month, is unmarried. Support for marriage and the family is a cardinal value promoted by both the Christian Democrats and by their Bavarian and predominantly Catholic sister party, the Christian Social Union, which Mr Stoiber heads. Many conservatives, along with representatives of the German Women's Union and the Catholic Church, are aghast. Some suggest removing the family from Ms Reiche's responsibilities. Others protest that an unmarried mother should not be in Mr Stoiber's team at all.

Among northern Europeans, Germans bear relatively few children out of wedlock—just 23% of births, compared with some 40% in Britain, France and Finland, and more than half in Sweden (see chart). Germany's constitution specifically protects "marriage and the family". On the campaign stump, Mr Stoiber proudly announces that he has been married to the same woman for 34 years—"unlike some", he sometimes adds, in a thinly disguised dig at the current chancellor, Gerhard Schröder, who is on his fourth marriage. Many conservatives castigated a new law giving gay couples the same welfare and inheritance rights as married couples, because—they said—it undermined marriage.

Not all conservatives are old-fashioned. The Christian Democrats' own party leader, Angela Merkel, lived with her partner for 17 years before marrying him in 1998. And Mr Stoiber knows it is electorally wise to move with the times. While still upholding marriage as the ideal, he now says that "other forms of partnership" should be "accepted and respected". The unmarried Ms Reiche is modern, bold, ambitious. That, he is convinced, will go down well with voters. Despite the rumpus, he is standing by her; he could do little else, without reinforcing the right's fuddy-duddy reputation.

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Charlemagne

# Farmer Franz Fischler

Jul 4th 2002
From The Economist print edition

**Can the European Union's canny agriculture commissioner reform its ghastly farms policy?**

A FEW years ago Franz Fischler astonished the dignitaries at a European farm ministers' meeting in Biarritz by tramping through the lobby of a posh hotel in a tiny swimming costume after a bracing dip in the Atlantic. It was an impressive act of bravado from the Union's amply-proportioned agriculture commissioner. However grumpy the mutterings behind his back, he will need all his guts and skill to press ahead when, on July 10th, he unveils his proposals for reforming the EU's famously costly and protectionist common agricultural policy (CAP).

Early drafts of Mr Fischler's ideas have been hailed as likely to create a radical upheaval in the CAP. Traditional beneficiaries of farm subsidies, such as France, have made it plain they will oppose much of what he is suggesting. The most far-reaching idea is to cut the links between subsidies and production. EU farmers will still get plenty of public cash thrown at them but the money will no longer be tied to how much beef or grain or oil-seed rape they produce. Farmers will be guided by the demands of the market in deciding what to grow. Their new subsidies will be linked to environmental and animal-welfare standards and cut by a fifth in stages, with the savings redirected towards rural development. And in future, rural-development projects will have to be co-financed by the countries that benefit from them rather than all be paid out of a central pot in Brussels. The end product, it is hoped, is an agriculture policy more oriented towards consumers and less to big farmers.

Mr Fischler's proposals will be controversial. “If there wasn't a big fight over agricultural reform,” he notes, “people would think there was something wrong.” But don't exaggerate the radical nature of his plans. He assumes without question that farming deserves to be subsidised. Nor does he propose an overall cut in the enormous amount of money that goes into the CAP, which at *euro*40 billion amounts to almost half of the EU's overall spending. “I'm not a revolutionary,” Mr Fischler notes carefully.

Despite his jovial manner and background in Austria's conservative mainstream, he is not just a straightforward Tyrolean farmer; his bluff exterior hides a shrewd political brain. When Austria was virtually isolated in EU politics after the far-right Freedom Party joined the government in 2000, Mr Fischler said just the right things to preserve his political viability both in Brussels and in conservative circles in Vienna. Now he is trying to use the same skills to steer through CAP reform, a subject that has led to bitter rows between France and Germany and between northern and southern Europeans—and is now further complicated by the imminent enlargement of the EU to include poorer and more rural countries in Central Europe.

The strategy behind the proposals is evident in the way Mr Fischler proposes severing the link between production and subsidy. The simplest idea would be to move to an “area payment”, with farmers getting money based on the amount of land they farm. But that idea would be immediately shot down by the French, who, because they farm intensively, do very well out of production-based subsidies and would be hurt by a simple move to area payments. Instead, Mr Fischler is trying to disarm opposition by proposing that all farmers should start with the same level of subsidy they got under the old system but that the amount paid to the biggest farms should be capped and then progressively reduced. In this way Mr Fischler hopes gradually to address one of the most widely criticised of the CAP's anomalies: the fact that a policy often defended as a way of protecting small farms and traditional rural life in fact lavishes around 80% of its subsidies on just 20% of the EU's largest farms.

Mr Fischler's wiles are apparent in other bits of his proposals. For the time being, “Mediterranean products” like wine and olive oil are exempt from the proposed abolition of production subsidies. These markets, says Mr Fischler, are not yet ready for so radical a move; he will bring forward proposals for them next year. Conveniently for him, this means that the Spaniards, Italians and Greeks are less likely

to join a militantly anti-reform camp. Mr Fischler's proposals are also meant to give countries like Germany, Britain and the Netherlands, which grumble that they foot the CAP bill, just enough to win him their backing. For the northerners Mr Fischler emphasises that his is a market-based reform that will benefit consumers and the environment, and will eventually lessen their payments. For the French and the southerners, he stresses that he does not question the need to preserve a subsidised “European model” of farming. His strategy, he says with a smile, is to find a “balance of unhappiness”.

He applies the same idea to countries such as Poland and the Czech Republic, which are banging on the door of the EU but are increasingly nervous that they will be offered a rotten deal over agriculture. Mr Fischler agrees with the applicants that the EU's efforts to reform the CAP should on no account stand in the way of enlargement; but he also sticks to the European Commission's line that the newcomers cannot expect to get the full range of agricultural subsidies as soon as they join.

## Tyrolean tiptoes

This carefully calibrated strategy worries those who are agitating for a really radical CAP reform. They are concerned, in particular, that if the amount of money spent on the CAP is not cut before eastward enlargement, the new farmer-heavy members may form an anti-reform block once they are inside the Union. Mr Fischler shares the reformers' view that in the long run farm subsidies cannot stay the biggest single item in the EU's budget. But he argues that the budget will have to be reshaped after a post-enlargement deal is struck, with aid to poor regions going up sharply as farm subsidies shrink. EU history suggests that agricultural reformers invariably enter cold and treacherous waters. Mr Fischler may have a risqué bathing suit, but his style is to walk in step by step, not to plunge head first into the waves.

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**Britain and America**

# Listen, George

Jul 4th 2002
From The Economist print edition

Rex

**Tony Blair has staked a lot on his relationship with George Bush. That makes recent snubs particularly damaging to Mr Blair**

NOBODY doubts that the “special relationship” between Britain and America is going through a rough patch. But is it, as Jack Straw, the foreign secretary, insisted this week, merely a question of one or two disagreements between friends? Or is it the harbinger of something more serious going wrong in a relationship that in the immediate aftermath of September 11th seemed as close as at any time since the second world war?

There is certainly no shortage of friction points. On trade issues, where the Bush administration was expected to be instinctively sound, the farm bill and the steel tariffs have caused profound disappointment. The president's refusal to listen to Tony Blair's repeated pleas at last weekend's G8 meeting in Canada to cut him some slack on steel was especially galling.

To the many who believe that the International Criminal Court (ICC) is as close as it gets to being a good deed in a bad world, America's wrecking tactics on the eve of its inauguration were shocking. They demonstrated the same disdain for multilateralism that had led to its rejection last year of the Kyoto climate-change treaty (also strongly supported by Britain). And when President Bush finally outlined his ideas on a Middle East peace process, British diplomats were dismayed by his insistence that progress was conditional on the Palestinians dumping Yasser Arafat.

Even in Afghanistan, there are now said to be divisions over the conduct of the war. According to one story (sourced to “senior officials in the prime minister's office”, but vehemently denied) there are growing concerns over the crudeness of the tactics the Americans are employing to hunt down the remaining al-Qaeda terrorists. This week's attack on a Pathan wedding party only added fuel to the rumours.

**Mr Blair remains closer to the open and straightforward Mr Bush than he ever was to the more obviously like-minded Bill Clinton**

The prime minister, like Mr Straw, is publicly dismissive of all this. He says that the relationship is no different from what it has always been, “solid, sound and working well”. But of course, he would say that. As one close colleague put it: “If Tony was writing out his job description, near the top of the list would be having a close relationship with the president.” And he does indeed seem to have achieved that. To the surprise of many, Mr Blair remains closer to the open and straightforward Mr Bush than he ever was to the more obviously like-minded Bill Clinton.

But political leaders always like to claim “personal chemistry” with each other; and experienced observers of British-American relations are worried. The problem, they say, is that nothing, not even the war

against terror, has replaced the cold war security relationship. That relationship, they say, was so fundamental to both sides that disharmony over other issues hardly mattered. A former American ambassador to Britain wistfully recalls: “It gave us clarity and structure, a shared vocabulary and agenda.”

These days, political pressures on Washington and London matter far more than they used to. Mr Bush and Mr Blair may get on, but they have to appeal to constituencies that are poles apart. And whatever the chumminess at the top, there is no guarantee that it extends to officials lower down the chain of command. Before September 11th, few would have predicted such a pivotal role for the hawkish ideologues who Mr Bush sent into top posts at the Pentagon. It's fair to say that Donald Rumsfeld's fan-base is somewhat narrower in Britain than in America.

Not that recent divisions are explicable simply in terms of a conventional left-right split. Britain's Tories support the ICC, while Mr Clinton was lukewarm. Attitudes to sovereignty in Europe—including Britain—are different to those in America. The Europeans have come to accept the idea that pooling sovereignty can deliver benefits. Americans think that sovereignty is something to be vigorously defended, and relinquished only reluctantly (if at all). Incomprehension over the ICC is therefore genuine and mutual. And for all the backslapping bonhomie between Mr Bush and Mr Blair, the two men perfectly represent the difference: Mr Blair is the quintessential liberal internationalist, while Mr Bush is intuitively a conservative unilateralist. Both men may be interventionists, but Mr Blair has a dreamier view of such things than does Mr Bush.

That said, many people are probably exaggerating the extent of the disagreements between America and Britain. Mr Blair sees himself as attacked from both sides of the political divide: by the Conservative right, which cannot bear to see him working well with their hero; and by the old left, whose atavistic anti-Americanism is agreeably fed by Mr Bush's moral certainty and verbal clumsiness. And, in truth, trade disputes with America are nothing new, while the gap between Mr Bush and Mr Blair over the Middle East is of nuance more than substance. As one of the prime minister's close advisers says of Mr Bush's Middle East speech: “Tony might have used different language, but he agrees that Arafat is a guy you can't deal with.”

But that doesn't alter the fact that Mr Blair does have a real problem at home. The perception that he gives unquestioning support to the United States and that Britain gets nothing in return is strong and growing. When Mr Blair talks about the influence that such support buys and the benefits that Britain gets from the intensity of the military and intelligence relationship, it cuts little ice. If, as is plausibly claimed, Mr Blair helped shape the Bush administration's enlightened policy towards Russia by convincing the president that Vladimir Putin was much more than a former KGB goon, or that Britain and America worked hand in hand to stop India going to war with Pakistan, the prime minister will get small credit for it. Having ceded much of the domestic policy agenda to the chancellor, Gordon Brown, Mr Blair needs to claim successes that impinge more directly on Britain's national interest.

**The perception that Mr Blair gives unquestioning support to the United States and that Britain gets nothing in return is strong and growing**

Should this be of any concern to George Bush? Perhaps not much, at least for now. But if he does decide to go to war with Iraq this winter (admittedly still a big “if”), even people in the White House and the Pentagon concede that being able to say “the Brits are with us” will be of great political importance to the president. The overwhelming likelihood is that Britain will be there, shoulder to shoulder as usual, no matter what additional snubs Mr Bush chooses to administer in the meantime. But with each one, he should realise that the decision on Iraq becomes just a little harder and a little riskier for his buddy, Tony.

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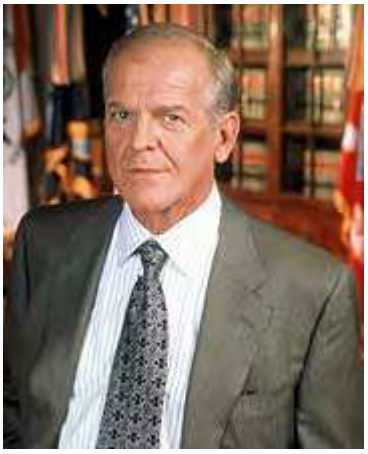
Politics and television

# Unreality TV

Jul 4th 2002
From The Economist print edition

**Irreverent television is good for politicians**

AMERICAN television viewers tend to have more glamorous tastes than their British counterparts. Their doctors, lawyers and detectives are obliged to be sexy as well as proficient; their soap operas requite the audience's fantasies (wealth, power, ultraviolence, and so on), whereas British soap characters spend their time in pubs and launderettes. The contrast is especially sharp in political drama—which helps to explain the popularity in high places of “The West Wing”, a recent television import.



**Leo sprinkles stardust on Downing Street**

Fictional American presidents wrestle with hijackers and repel alien invasions. Fictional British politicians are generally either buffoons (as in “Yes, Prime Minister”, a comedy that many civil servants think should be required viewing for politics students), or homicidal machiavels. Westminster politicians can look forward to the BBC's release of two new political dramas: one about the moral compromises incurred in getting and wielding power; the other about the murder of an intern.

So it's not surprising that Number 10 has looked west for encouragement. “The West Wing” is set in the eponymous White House corridors of power. It manages to be both sophisticated and saccharine: despite all the issue-handling and wisecracks, it is essentially a fairy-tale about a benign ruler. The president is devout but tolerant; a loving father who struggles manfully with Gordian policy knots—which he always unravels, as the music swells.

All of which evidently goes down well with affection-starved New Labourites. The actor who plays the grizzled chief-of-staff, Leo, visited Downing Street last week. A screening of the first issue of the new series was thronged with MPS, including several ministers.

Critics of Blairism might detect something sinister in this latest trans-Atlantic crush. After all, “The West Wing” portrays a coterie of ruthlessly disciplined unelected advisers (much like the denizens of Downing Street). The fictional spin-doctors occasionally distort or make up the news—though always in a noble cause (unlike, critics of Blairism might say, their real-life British avatars).

Perhaps Americans have been driven to such fantasies by the tawdriness of real-life politics. Or perhaps they revere the presidency while disdaining actual presidents. Either way, all that on-screen idolisation doesn't get them to the polls: presidents get elected with around a quarter of the vote (give or take a few pregnant chads). In Britain, where television sets them much lower standards, politicians may seem not quite as reprehensible as their fictive counterparts. So maybe Blairites should view “The West Wing” less as flattery than as a dangerous boost to public expectations.

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Currencies and xenophobia

# Many a true word...

Jul 4th 2002
From The Economist print edition

**One currency, one bad joke, one national obsession**

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Reuters

**The zany, madcap Führer**

THERE is a tactic commonly used in political and moral arguments that might be described as “the Führer manoeuvre”. In it, Hitler serves as a sort of rhetorical trump. Back a critic of cloning into a corner and sooner or later (but probably sooner) he'll reach for a Nazi analogy. Advocate immigration controls? You sound like Adolf. In a similar vein, opponents of British entry into the single currency have enlisted the Führer to their cause.

He appears in an advert soon to grace British cinemas, which is expected to be seen by 5m people. Aimed at the yoof market, it begins with an allusion to a more contemporary metaphor for disastrous political hubris, the Millennium Dome. A procession of zeitgeisty comedians then share their views on macroeconomics. To prove how respectably trendy and tolerant it is to hate the euro, the ad features a clutch of actual foreigners, and Bob Geldof, a minor Irish pop star turned latter-day charitable saint. More importantly, there are no Tories in sight. The euro is presented as a rich man's folly; the “bureaucrats in Brussels” make their inevitable appearance.

The controversial part comes when one of the funny-men dresses up as Hitler to declaim “Ein Volk, Ein Reich, Ein Euro!”. The anti-euro campaign, which produced the advert, says the Hitler segment was intended only as “zany, madcap comedy” (though Jewish groups, war veterans and the German embassy failed to see the joke). Beneath the zaniness, though, this is a classic example of the Führer manoeuvre: Hitler would have liked the euro, it suggests; so you shouldn't.

The pro-euro camp—which contains more statesmen, but fewer comedians—has confidently predicted that the Nazi skit will damage their adversaries, by revealing the past-bound little-Englander motivations of the euro's enemies. But perhaps they are too confident—because the truth is that many British voters are past-bound Hitlerphobes. One anthem of choice for England's football fans at the World Cup was the theme tune to “The Great Escape”—a film about a mass outbreak from a German POW camp. The fans' band played this hymn to resilience amid adversity even when England were winning. Nazism dominates the nation's history lessons and historical television documentaries. Lots of people do think the euro is a German plot to put a monetary, but nonetheless Teutonic roof over Europe.

Both sets of euro-warriors claim to want an honest debate about the single currency. Since the outcome of any referendum will partly depend on the persistence or otherwise of atavistic fear and loathing, in a funny (or not so funny) way, the Fuhrer manoeuvre has identified one of the things they need to discuss.

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Hotel prices

# Chequing in

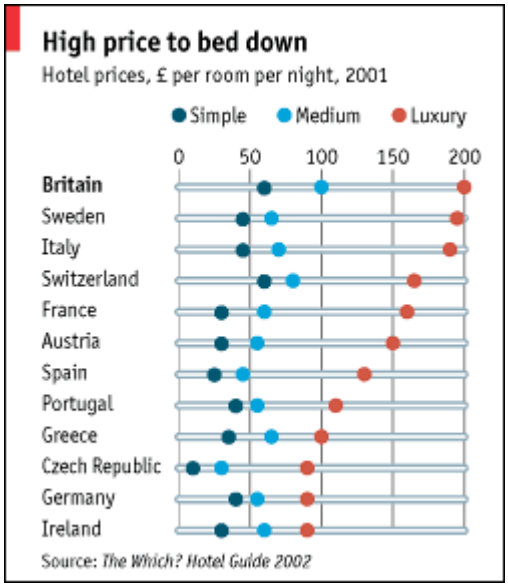
Jul 4th 2002 | EAST PORTLEMOUTH, DEVON, AND LONDON
From The Economist print edition

**Why are Britain's hotels so expensive?**

IN THE aftermath of the foot-and-mouth crisis, Kim Howells quipped that a lot of British hotels "make 'Fawlty Towers' look like a documentary". Not the sort of thing you'd expect to hear from the tourism minister. But he's got a point. Your recently married correspondent, for one, is still reeling from a hotel honeymoon of unforgettable, unutterable awfulness—a stunning exhibition of incompetence on every level, from grubby crockery and dysfunctional plumbing to a service ethos that would have made Basil himself cock an admiring eyebrow.

Such experiences don't come cheap. According to the "Which? Hotel Guide 2002", British hotels are the most expensive in Europe, from the lowliest doss-house up (see chart). The situation is especially bad in London, where a shortage of hotel rooms, coupled with strong demand, keeps prices sky-high. "You can find a good, individual hotel in the middle of Paris for *euro*60 a night," says Patricia Yates, co-editor of the "Which? Hotel Guide", "but I wouldn't like to try to find one at that price in London—or to have to stay there."

The strength of the pound is often blamed. VAT is certainly a factor: at 17.5% it is the second highest in Europe, after Denmark. Elsewhere it hovers between 3% and 10%. But any independent hotelier will tell you that it is above all the cost of property that accounts for the scarcity of well-designed, moderately priced, owner-run hotels in central London.




Peter McKay, who co-owns two of the city's finest small hotels—Hazlitt's in Soho and The Gore in Kensington—says the problem starts with finding a suitable building. "You're going to need between 25 and 55 rooms," he says. "In the West End, that means an outlay of £6m-7m on the property alone." After successfully fending off competition from residential and commercial bidders, gaining the necessary planning permission and converting the existing building from top to bottom, all according to strict building regulations, you could easily be looking at a capital investment of £10m ($15m).

"And then," says Mr McKay, "there are the rates." Commercial property rates are calculated according to an arcane formula whose secrets, it seems, are fully understood only by a select few initiates among the bureaucratic brotherhood. Those hoteliers who have the wherewithal to do so regularly challenge their assessment. This can save them hundreds of thousands of pounds—underscoring the apparent arbitrariness of the whole process.

No wonder, then, that most London hotels are run by multinational chains. Continental Europe, by contrast, still has a strong tradition of independent hotels, many of which remain in the same family for generations, and can thus operate with a lot less pressure from bank managers or shareholders.

Mr McKay has nothing against corporation-owned hotels; he just doesn't want to run one himself. A really good hotel, he believes, bears the personal imprimatur of its owner—it should reflect his or her "commitment to the *thing*". Flexibility is the key. "The nearer you are to your customers, the easier it is to be flexible." That can affect every aspect of how you do business—from the overall look and feel of a hotel to its willingness to serve butter on a dish instead of in a packet. Not for Mr McKay the dead hand of chain-hotel sameness. This sentiment is one his Continental counterparts would recognise

immediately—*vive la différence*.

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Housing in the south-east

# Gordon versus the nimbies

Jul 4th 2002
From The Economist print edition

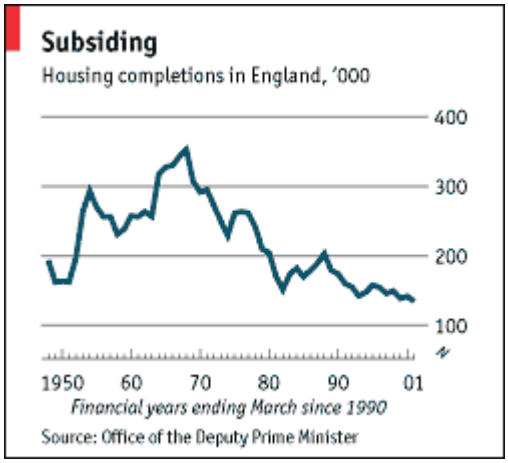
**Higher immigration and less house-building are pushing prices up**

IN HIS speech to the City last week, Gordon Brown, the chancellor, made clear one of the priorities for his forthcoming spending plans. The plans, he said, would “take seriously the case for further new housing development”. He also called for “radical planning, housing and transport reforms” to underpin the growth prospects of London and the south-east.

The need to do something about Britain's runaway housing boom was highlighted this week when the Nationwide Building Society revealed that the price of a typical house had risen by 3.3% in June alone—and by almost 20% in the past year. Although the boom is spreading north, house-price valuations remain most overstretched in London and the south-east.

One reason why the housing market is so buoyant is the shortage of new homes. In 2000-01, the number of new homes completed in England fell to 134,739, its lowest since 1947—rather less than the 193,000 new homes needed every year to meet the growth in new households and to replace existing housing stock. The most serious shortfall is in London and the south-east, where unusually high levels of immigration have pushed up the rate of household formation. Alas, economics and politics are at odds. The economics point to a relaxation of planning controls. London and the south-east are Britain's growth engine. It would be desirable if some of the growth could be diverted north; and higher house prices will contribute to that process. But the fear is that some potential growth may simply be lost for good if companies find they cannot operate effectively in the south-east.

Politics, on the other hand, urge caution. There are, after all, good reasons for people to be nimbies. “The more people have paid to fight their way into the shire counties the more they've got to lose from a relaxation in planning controls,” says Tony Champion, professor of population geography at Newcastle University.




There appear to be two major, nimbyish reasons for the current building shortfall. Councils, under pressure from residents, resort to a variety of delaying tactics to thwart development. And the government is now committed to develop 60% of new housing on brownfield sites. This in itself was a concession to nimbyism. However, the policy is backfiring. Sir Peter Hall, professor of planning at University College London, says that “the brownfield policy has proved to be a disaster because it is not delivering the land necessary to meet the government's overall housing targets.” One explanation is that developers are deterred by the cost of cleaning up brownfield sites, which in any case are often in undesirable urban areas.

Any strategy to deal with the shortfall would have to be multi-faceted. One step could be to make regional planning targets binding upon councils. For example, the House Builders Federation calls for financial sanctions on councils that do not meet agreed targets for new homes. The Town and Country Planning Association,which once advocated new towns, now calls for large-scale “whole community” development—new towns by a new name. It also thinks that the present system of tax relief for developers who clean up brownfield sites is inadequate, and advocates a government-financed clean-up programme.

All this would be costly, either financially or politically. Cleaning up contaminated land is expensive. Sanctions against councils would surely cause an outcry. Already, the government's proposals to simplify

and speed up the planning regime especially for major infrastructure projects have met widespread opposition.

On past evidence, politics will prevail. In 1999, a panel of government-appointed planning inspectors called for a 20-year programme of 55,000 new homes a year in the south-east. Such was the hostility of local councils and residents that the government eventually settled on 39,000. As Sir Peter says, the government backed down “because it feared a voter backlash in marginal constituencies”. Those marginal constituencies haven't gone away.

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**Railways**

# Puff, puff

Jul 4th 2002
From The Economist print edition

### High-speed trains are coming, but very slowly

Get article background

HALF a century ago, the Mallard set a world speed record for a steam train of 126mph. When the new so-called “super-fast” tilt trains come into service on the upgraded West Coast main line between London and Glasgow in May 2004, they will travel marginally slower than the pre-war record-breaking puffer.

High-speed lines, increasingly common in the rest of the world, are still unknown in Britain. The Channel Tunnel Rail Link will be the first. Later this year the Strategic Rail Authority (SRA), which plans the railway's future, will publish a detailed study into the commercial viability of a high-speed (225mph) rail line from London to the north.

The £1.3m study by a firm of consulting engineers, WS Atkins, is understood to support the case for a high-speed line. It would cut the journey time from London to Manchester from two hours 40 minutes to less than 90 minutes by 2015. Richard Bowker, the SRA's chairman, likes the idea and believes it will cut congestion on the national network. The new line will probably run through open country, possibly following the route of the old, now disused, central railway which cuts midway between the west and east coast main lines. It would then link up with existing track going into city centres.

The main argument in favour of a dedicated high-speed line is that demand for travel is certain to increase, and cannot be met by either roads or airlines, both of which are already heavily congested. Even if sufficient new airport and motorway capacity could be built, high-speed rail is more reliable, energy-efficient, comfortable and safer than competing forms of transport. The Japanese *shinkansen* (bullet) trains have carried more than 3 billion people with impeccable punctuality and safety over the past three decades. Delays are measured in seconds. Not a single passenger has been killed since the *shinkansen* began operating in 1964.

For journeys of between 100 and 400 miles, high-speed rail is also usually quicker for travellers going to city-centre destinations. The case for a new high-speed line in Britain has been strengthened by the doubling in cost of improvements to the West Coast main line. It is much easier and less risky to build a new railway than to try to patch up an old one.

High-speed lines invariably require large amounts of government support. But their environmental, social and regional benefits have persuaded many European countries that they are worth it. The Spanish AVE does the 300 miles from Madrid to Seville in two hours. The French *Train à Grande Vitesse* (TGV) cruises at 185mph from the Channel coast to the Riviera. Germany's Inter-City Express (ICE) does the 70-mile journey from Göttingen to Hanover in less than half an hour. More than a dozen high-speed railways are under development around the world. Even the United States, with its aversion to projects financed with public money, has new trains connecting Washington and Boston that can in theory go at 150mph, though the track is in poor condition.

The only proven case of a self-financing high-speed line is the Tokyo to Osaka route. Its profits cover both interest and operating costs. It it is also formidably competitive. High-speed *shinkansen* depart from Tokyo bound for Osaka every five minutes at rush hour. There are now six times as many trains on the route as there are airline departures, and the *shinkansen* have more than 80% of the market.

A British high-speed line could not be expected to do as well. The price would also be formidable. The Channel tunnel rail link, which is due to come into service in 2007, is costing £5.5 billion for just 70 miles of track. The Treasury will rightly want to be convinced not only that the economics make sense, but also that the railways have put their house in order. Postponing a decision is not, however, a painless option. High-speed lines take a generation to build, and it is no good waiting until the country grinds to a halt.

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Digital television

# The odd couple

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From The Economist print edition

**Broadcasting's curious duopoly: the BBC and BSkyB**

THIS was the BBC's nightmare: that on the day the analogue signal was switched off and even BBC1and BBC2, its free flagship channels, were only available digitally, their transmission would be controlled by Britain's most powerful pay-TV operator, Rupert Murdoch's BSkyB, because Sky owned the most powerful digital platform. So the decision by the Independent Television Commission to award the BBC the old ITV Digital licence for the next 12 years frees it from such a future. The oddity is that, as a result, the BBC has jumped into bed with the bogeyman.

If further proof were needed that digital television in Britain is being carved up neatly between the BBC and BSkyB, then this decision would seem to be it. BSkyB is by far the dominant supplier of digital TV. With 5.7m pay-TV subscribers, all of them receiving their channels digitally, it dwarfs its debt-laden cable competitors, NTL and Telewest. Until now, the BBC's digital-only channels, such as BBC4 and two children's channels, were available only through one of the pay-TV operators. Now, anybody who buys a digital set-top box, currently on sale for around £100, will be able to receive them, and a few others, such as QVC, a shopping channel, free. No dish, no monthly subscription. The BBC hopes to supply 5m households within six years.

For the BBC, getting its hands on a means of digital TV distribution is a coup. It will not only put the future of its own channels firmly back in its own hands, but will provide a strong incentive for marketing its poorly watched digital channels. A top-rated BBC4 programme, for instance, such as “Maya Angelou at Hay-on-Wye”, gets about 30,000 viewers, next to the 1m or so who tune in to “The Simpsons” on Sky One. The immediate gains for Sky are less significant. It is throwing only three of its least valuable channels into the free package—Sky News, Sky Sports News and Sky Travel—and keeping the top sports and movie channels that lure its subscribers firmly to itself. But it will be a useful way to get viewers to sample its wares.

The BBC insists that it is not cramping its competitors. Its service is designed, it says, for people who do not want pay-TV. While they will not initially be able to upgrade to pay-TV from the free version, Greg Dyke, BBC's director-general, says that he might consider making this possible “in the long term”.

The upshot will be the entrenchment of Sky and the BBC as the fellow kings of digital TV. And for that, the BBC has in large part to thank the ITV companies, which backed the strongest rival bid for the licence awarded this week, but whose credibility was destroyed by their spectacular failure with ITV Digital.

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Bagehot

# Happy birthday, BT

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From The Economist print edition

**The government's refusal to let telecoms alone says a lot about its attitude to the private sector**

TWENTY years ago this month, Margaret Thatcher's government embarked on what was at that stage its boldest experiment with the announcement that it intended to sell a 51% stake in the state-owned telephone company, British Telecommunications. “Privatisation”, as the transfer of public enterprises to private-sector ownership and control became known and a term, Bagehot can brag, invented by Norman Macrae, then deputy editor of this organ, grew into Britain's most successful policy export since parliamentary democracy.

Not that you'd think it from attitudes at home. To start with, the very idea of introducing competition was regarded as perverse by the telecoms establishment. Almost everybody was against it, from MI5, which worried about its ability to keep track of subversives, to the unions, who warned that armies of engineers would face electrocution. But it is the government's attitude today that is most worrying. Twenty years on, the government is run by Labour, and it says it favours competition. But does it? There is still no consistent view about the proper relationship between normal competition policy and the sectoral regulation that was invented to deal with the particular problems caused by the former nationalised monopolies. As BT's story shows, the habit of regarding an industry regulator as a means of micro-managing an industry rather than establishing competitive markets lingers on.

For all their supposed Thatcherite zeal, the Conservatives never set much of an example. The government's main aims were to shift the burden of financing BT's new digital exchanges to the private sector and to make a killing for the Treasury. A competitive telecoms market, and the benefits it would bring to consumers, could come later. The result was the so-called “duopoly”—a seven-year settlement during which the only firm allowed to compete with BT was the fledgling Mercury, a division of Cable & Wireless.

That had two unfortunate consequences. The first was to create a precedent for the nascent mobile-phone industry in which a similar duopoly between BT's Cellnet and Vodafone was allowed to persist until 1993. The predictable outcome was a snug little cartel that kept prices high and service innovation low for too long. The second was that another set of newcomers, cable-television operators, came close to being strangled at birth. The government, egged on by BT, decreed that they should not be allowed to offer voice and data services over their networks and could have access to no more than 5m homes each. Belatedly, the government relented but the effort to consolidate the industry and develop a rival telephony service to BT has financially crippled and strategically distracted the two survivors, Telewest and NTL.

It wasn't until the appointment of a tough new director-general of the Oftel watchdog in 1993, Don Cruickshank, that a coherent framework for promoting a competitive telecoms market began to emerge. Mr Cruickshank saw that the key to this was to establish a set of rules governing interconnection to BT's network that were transparent and economically attractive to new entrants. Without it, the investment to create the scale needed to take an incumbent on would never be forthcoming. Oftel under Mr Cruickshank became the model for other countries in Europe as they liberalised their telecoms markets.

## Fiddle, fiddle, fiddle

The measure of Mr Cruickshank's success in advancing a normally functioning market is that by the time he left, five years later, the proportion of BT's revenues that Oftel regulated had fallen from 60% to 18% and control over BT's retail pricing was no longer deemed necessary. With a far-reaching competition act

passed in 1998, Mr Cruickshank hoped that micro-regulation of specific industries would soon be superseded by a general set of competition rules.

It was a nice idea, but hopelessly over-optimistic. As one former regulator put it: “New Labour intellectually understood that competitive markets were needed, but they can't resist grabbing, influencing and controlling everything themselves.” The government's gyrations over broadband Internet connections are a case in point. After the prime minister announced that it was vital for Britain to become a world leader in “e-business”, it became an obsession to speed up the rate of broadband adoption. Instead of setting itself the objective of continuing with Mr Cruickshank's work in developing a genuinely competitive telecoms market, the object of policy was something that became known as “Broadband Britain”.

What followed was a doomed attempt by the current director-general at Oftel, David Edmonds, to choreograph the market into dancing to the government's tune. Mr Edmonds convinced himself that the key to stimulating the market for high-speed Internet was to force BT to allow rival companies to install their gear into its exchanges. BT, always better at dealing with the regulator than at running its business, dug in and delayed until its cash-strapped would-be competitors lost heart or went bust. The irony is that if the government had just concentrated on promoting competition rather than trying to implement a half-baked industrial policy, “Broadband Britain” might be a little closer to reality than it actually is.

If Oftel has become a shambles, the new Ofcom that the government is setting up to oversee the entire communications industry looks like being even more flawed than the agencies it is replacing. With responsibilities for taste and broadcasting standards added to its competition remit, it cannot but be deeply confused about its purpose. The government probably knows what it should do—retreat from sectoral regulation and rigorously enforce just one set of tough competition rules for every industry. But can a fish ride a bicycle?

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# The great race

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**Growth need not be the enemy of greenery. But much more effort is required to make the two compatible, says Vijay Vaitheeswaran**

SUSTAINABLE development is a dangerously slippery concept. Who could possibly be against something that invokes such alluring images of untouched wildernesses and happy creatures? The difficulty comes in trying to reconcile the “development” with the “sustainable” bit: look more closely, and you will notice that there are no people in the picture.

That seems unlikely to stop a contingent of some 60,000 world leaders, businessmen, activists, bureaucrats and journalists from travelling to South Africa next month for the UN-sponsored World Summit on Sustainable Development in Johannesburg. Whether the summit achieves anything remains to be seen, but at least it is asking the right questions. This survey will argue that sustainable development cuts to the heart of mankind's relationship with nature—or, as Paul Portney of Resources for the Future, an American think-tank, puts it, “the great race between development and degradation”. It will also explain why there is reason for hope about the planet's future.

The best way known to help the poor today—economic growth—has to be handled with care, or it can leave a degraded or even devastated natural environment for the future. That explains why ecologists and economists have long held diametrically opposed views on development. The difficult part is to work out what we owe future generations, and how to reconcile that moral obligation with what we owe the poorest among us today.

It is worth recalling some of the arguments fielded in the run-up to the big Earth Summit in Rio de Janeiro a decade ago. A publication from UNESCO, a United Nations agency, offered the following vision of the future: “Every generation should leave water, air and soil resources as pure and unpolluted as when it came on earth. Each generation should leave undiminished all the species of animals it found existing on earth.” Man, that suggests, is but a strand in the web of life, and the natural order is fixed and supreme. Put earth first, it seems to say.

Robert Solow, an economist at the Massachusetts Institute of Technology, replied at the time that this was “fundamentally the wrong way to go”, arguing that the obligation to the future is “not to leave the world as we found it in detail, but rather to leave the option or the capacity to be as well off as we are.” Implicit in that argument is the seemingly hard-hearted notion of “fungibility”: that natural resources, whether petroleum or giant pandas, are substitutable.

## Rio's fatal flaw

Champions of development and defenders of the environment have been locked in battle ever since a UN summit in Stockholm launched the sustainable-development debate three decades ago. Over the years, this debate often pitted indignant politicians and social activists from the poor world against equally indignant politicians and greens from the rich world. But by the time the Rio summit came along, it seemed they had reached a truce. With the help of a committee of grandees led by Gro Harlem Brundtland, a former Norwegian prime minister, the interested parties struck a deal in 1987: development and the environment, they declared, were inextricably linked. That compromise generated a good deal of euphoria. Green groups grew concerned over poverty, and development charities waxed lyrical about greenery. Even the World Bank joined in. Its World Development Report in 1992 gushed about “win-win” strategies, such as ending environmentally harmful subsidies, that would help both the economy and the environment.

By nearly universal agreement, those grand aspirations have fallen flat in the decade since that summit. Little headway has been made with environmental problems such as climate change and loss of biodiversity. Such progress as has been achieved has been largely due to three factors that this survey will explore in later sections: more decision-making at local level, technological innovation, and the rise of market forces in environmental matters.

The main explanation for the disappointment—and the chief lesson for those about to gather in South Africa—is that Rio overreached itself. Its participants were so anxious to reach a political consensus that they agreed to the Brundtland definition of sustainable development, which Daniel Esty of Yale University thinks has turned into “a buzz-word largely devoid of content”. The biggest mistake, he reckons, is that it slides over the difficult trade-offs between environment and development in the real world. He is careful to note that there are plenty of cases where those goals are linked—but also many where they are not: “Environmental and economic policy goals are distinct, and the actions needed to achieve them are not the same.”

## No such thing as win-win

To insist that the two are “impossible to separate”, as the Brundtland commission claimed, is nonsense. Even the World Bank now accepts that its much-trumpeted 1992 report was much too optimistic. Kristalina Georgieva, the Bank's director for the environment, echoes comments from various colleagues when she says: “I've never seen a real win-win in my life. There's always somebody, usually an elite group grabbing rents, that loses. And we've learned in the past decade that those losers fight hard to make sure that technically elegant win-win policies do not get very far.”

So would it be better to ditch the concept of sustainable development altogether? Probably not. Even people with their feet firmly planted on the ground think one aspect of it is worth salvaging: the emphasis on the future.

Nobody would accuse John Graham of jumping on green bandwagons. As an official in President George Bush's Office of Management and Budget, and previously as head of Harvard University's Centre for Risk Analysis, he has built a reputation for evidence-based policymaking. Yet he insists sustainable development is a worthwhile concept: “It's good therapy for the tunnel vision common in government ministries, as it forces integrated policymaking. In practical terms, it means that you have to take economic cost-benefit trade-offs into account in environmental laws, and keep environmental trade-offs in mind with economic development.”

Jose Maria Figueres, a former president of Costa Rica, takes a similar view. “As a politician, I saw at first hand how often policies were dictated by short-term considerations such as elections or partisan pressure. Sustainability is a useful template to align short-term policies with medium- to long-term goals.”

It is not only politicians who see value in saving the sensible aspects of sustainable development. Achim Steiner, head of the International Union for the Conservation of Nature, the world's biggest conservation group, puts it this way: “Let's be honest: greens and businesses do not have the same objective, but they can find common ground. We look for pragmatic ways to save species. From our own work on the ground on poverty, our members—be they bird watchers or passionate ecologists—have learned that ‘sustainable use' is a better way to conserve.”

Sir Robert Wilson, boss of Rio Tinto, a mining giant, agrees. He and other business leaders say it forces hard choices about the future out into the open: “I like this concept because it frames the trade-offs

inherent in a business like ours. It means that single-issue activism is simply not as viable."

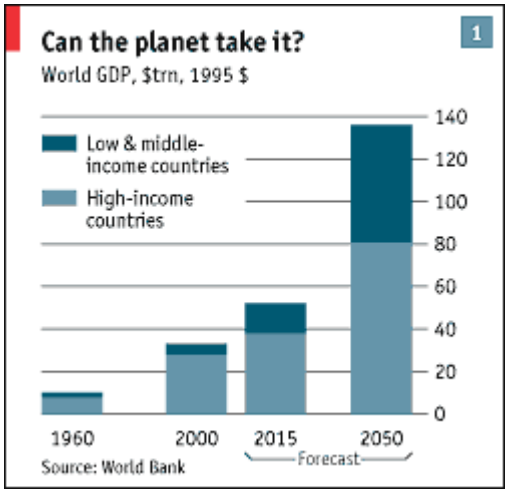
Kenneth Arrow and Larry Goulder, two economists at Stanford University, suggest that the old ideological enemies are converging: "Many economists now accept the idea that natural capital has to be valued, and that we need to account for ecosystem services. Many ecologists now accept that prohibiting everything in the name of protecting nature is not useful, and so are being selective." They think the debate is narrowing to the more empirical question of how far it is possible to substitute natural capital with the man-made sort, and specific forms of natural capital for one another.

## The job for Johannesburg

So what can the Johannesburg summit contribute? The prospects are limited. There are no big, set-piece political treaties to be signed as there were at Rio. America's acrimonious departure from the Kyoto Protocol, a UN treaty on climate change, has left a bitter taste in many mouths. And the final pre-summit gathering, held in early June in Indonesia, broke up in disarray. Still, the gathered worthies could usefully concentrate on a handful of areas where international co-operation can help deal with environmental problems. Those include improving access for the poor to cleaner energy and to safe drinking water, two areas where concerns about human health and the environment overlap. If rich countries want to make progress, they must agree on firm targets and offer the money needed to meet them. Only if they do so will poor countries be willing to co-operate on problems such as global warming that rich countries care about.

That seems like a modest goal, but it just might get the world thinking seriously about sustainability once again. If the Johannesburg summit helps rebuild a bit of faith in international environmental co-operation, then it will have been worthwhile. Minimising the harm that future economic growth does to the environment will require the rich world to work hand in glove with the poor world—which seems nearly unimaginable in today's atmosphere poisoned by the shortcomings of Rio and Kyoto.

To understand why this matters, recall that great race between development and degradation. Mankind has stayed comfortably ahead in that race so far, but can it go on doing so? The sheer magnitude of the economic growth that is hoped for in the coming decades (see chart) makes it seem inevitable that the clashes between mankind and nature will grow worse. Some are now asking whether all this economic growth is really necessary or useful in the first place, citing past advocates of the simple life.




"God forbid that India should ever take to industrialism after the manner of the West... It took Britain half the resources of the planet to achieve this prosperity. How many planets will a country like India require?", Mahatma Gandhi asked half a century ago. That question encapsulated the bundle of worries that haunts the sustainable-development debate to this day. Today, the vast majority of Gandhi's countrymen are still living the simple life—full of simple misery, malnourishment and material want. Grinding poverty, it turns out, is pretty sustainable.

If Gandhi were alive today, he might look at China next door and find that the country, once as poor as India, has been transformed beyond recognition by two decades of roaring economic growth. Vast numbers of people have been lifted out of poverty and into middle-class comfort. That could prompt him to reframe his question: how many planets will it take to satisfy China's needs if it ever achieves profligate America's affluence? One green group reckons the answer is three. The next section looks at the environmental data that might underpin such claims. It makes for alarming reading—though not for the reason that first springs to mind.

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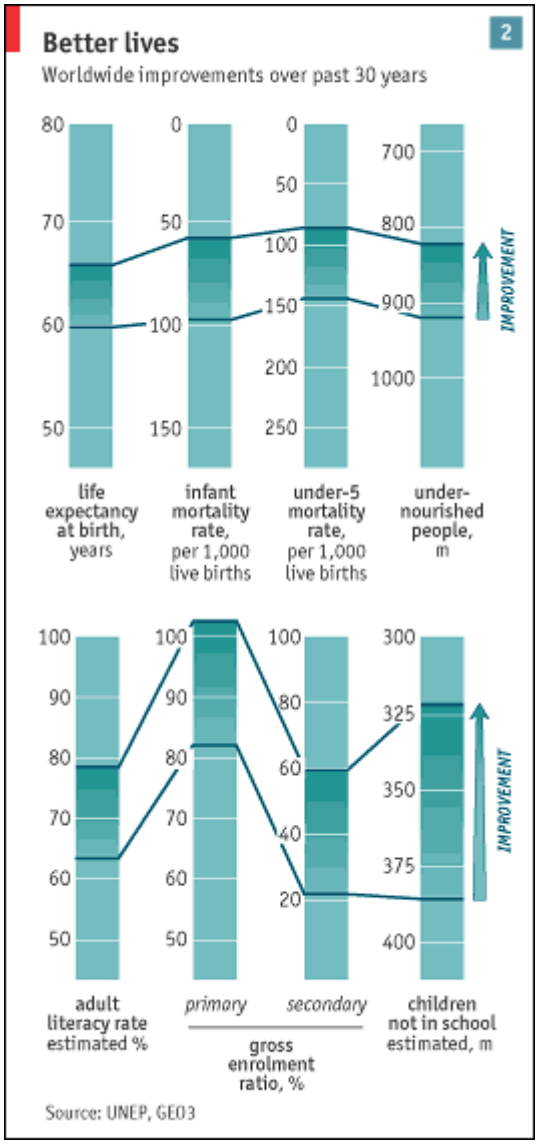
# Flying blind

Jul 4th 2002
From The Economist print edition

**It comes as a shock to discover how little information there is on the environment**

WHAT is the true state of the planet? It depends from which side you are peering at it. “Things are really looking up,” comes the cry from one corner (usually overflowing with economists and technologists), pointing to a set of rosy statistics. “Disaster is nigh,” shouts the other corner (usually full of ecologists and environmental lobbyists), holding up a rival set of troubling indicators.

According to the optimists, the 20th century marked a period of unprecedented economic growth that lifted masses of people out of abject poverty. It also brought technological innovations such as vaccines and other advances in public health that tackled many preventable diseases. The result has been a breathtaking enhancement of human welfare and longer, better lives for people everywhere on earth (see chart 2).




At this point, the pessimists interject: “Ah, but at what ecological cost?” They note that the economic growth which made all these gains possible sprang from the rapid spread of industrialisation and its resource-guzzling cousins, urbanisation, motorisation and electrification. The earth provided the necessary raw materials, ranging from coal to pulp to iron. Its ecosystems—rivers, seas, the atmosphere—also absorbed much of the noxious fall-out from that process. The sheer magnitude of ecological change resulting directly from the past century's economic activity is remarkable (see table 3).

To answer that Gandhian question about how many planets it would take if everybody lived like the West, we need to know how much—or how little—damage the West's transformation from poverty to plenty has done to the planet to date. Economists point to the remarkable improvement in local air and water pollution in the rich world in recent decades. “It's Getting Better All the Time”, a cheerful tract co-written by the late Julian Simon, insists that: “One of the greatest trends of the past 100 years has been the astonishing rate of progress in reducing almost every form of pollution.” The conclusion seems unavoidable: “Relax! If we keep growing as usual, we'll inevitably grow greener.”

The ecologically minded crowd takes a different view. “GEO3”, a new report from the United Nations Environment Programme, looks back at the past few decades and sees much reason for concern. Its thoughtful boss, Klaus Töpfer (a former German environment minister), insists that his report is not “a document of doom

and gloom". Yet, in summing it up, UNEP decries "the declining environmental quality of planet earth", and wags a finger at economic prosperity: "Currently, one-fifth of the world's population enjoys high, some would say excessive, levels of affluence." The conclusion seems unavoidable: "Panic! If we keep growing as usual, we'll inevitably choke the planet to death."

**A century that changed the world** 3

**Change between 1890 (=1) and 1990s**

| | |
|---|---|
| Industrial output | 40 |
| Marine fish catch | 35 |
| Carbon dioxide emissions | 17 |
| Energy use | 16 |
| World economy | 14 |
| World urban population | 13 |
| Coal production | 7 |
| Air pollution | 5 |
| Irrigated area | 5 |
| **World population** | **4** |
| Horse population | 1.1 |
| Bird and mammal species | 0.99 |
| Forest area | 0.8 |
| Blue-whale population | 0.0025 |

Source: "Something New Under the Sun" by John McNeill

"People and Ecosystems", a collaboration between the World Resources Institute, the World Bank and the United Nations, tried to gauge the condition of ecosystems by examining the goods and services they produce—food, fibre, clean water, carbon storage and so on—and their capacity to continue producing them. The authors explain why ecosystems matter: half of all jobs worldwide are in agriculture, forestry and fishing, and the output from those three commodity businesses still dominates the economies of a quarter of the world's countries.

The report reached two chief conclusions after surveying the best available environmental data. First, a number of ecosystems are "fraying" under the impact of human activity. Second, ecosystems in future will be less able than in the past to deliver the goods and services human life depends upon, which points to unsustainability. But it took care to say: "It's hard, of course, to know what will be truly sustainable." The reason this collection of leading experts could not reach a firm conclusion was that, remarkably, much of the information they needed was incomplete or missing altogether: "Our knowledge of ecosystems has increased dramatically, but it simply has not kept pace with our ability to alter them."

Another group of experts, this time organised by the World Economic Forum, found itself similarly frustrated. The leader of that project, Daniel Esty of Yale, exclaims, throwing his arms in the air: "Why hasn't anyone done careful environmental measurement before? Businessmen always say, 'what matters gets measured.' Social scientists started quantitative measurement 30 years ago, and even political science turned to hard numbers 15 years ago. Yet look at environmental policy, and the data are lousy."

## Gaping holes

At long last, efforts are under way to improve environmental data collection. The most ambitious of these is the Millennium Ecosystem Assessment, a joint effort among leading development agencies and environmental groups. This four-year effort is billed as an attempt to establish systematic data sets on all environmental matters across the world. But one of the researchers involved grouses that it "has very, very little new money to collect or analyse new data". It seems astonishing that governments have been making sweeping decisions on environmental policy for decades without such a baseline in the first place.

One positive sign is the growing interest of the private sector in collecting environmental data. It seems plain that leaving the task to the public sector has not worked. Information on the environment comes far lower on the bureaucratic pecking order than data on education or social affairs, which tend to be overseen by ministries with bigger budgets and more political clout. A number of countries, ranging from New Zealand to Austria, are now looking to the private sector to help collect and manage data in areas such as climate. Development banks are also considering using private contractors to monitor urban air quality, in part to get around the corruption and apathy in some city governments.

"I see a revolution in environmental data collection coming because of computing power, satellite mapping, remote sensing and other such information technologies," says Mr Esty. The arrival of hard data in this notoriously fuzzy area could cut down on environmental disputes by reducing uncertainty. One example is the long-running squabble between America's mid-western states, which rely heavily on coal, and the north-eastern states, which suffer from acid rain. Technology helped disprove claims by the

mid-western states that New York's problems all resulted from home-grown pollution.

The arrival of good data would have other benefits as well, such as helping markets to work more robustly: witness America's pioneering scheme to trade emissions of sulphur dioxide, made possible by fancy equipment capable of monitoring emissions in real time. Mr Esty raises an even more intriguing possibility: “Like in the American West a hundred years ago, when barbed wire helped establish rights and prevent overgrazing, information technology can help establish ‘virtual barbed wire' that secures property rights and so prevents overexploitation of the commons.” He points to fishing in the waters between Australia and New Zealand, where tracking and monitoring devices have reduced over-exploitation.

Best of all, there are signs that the use of such fancy technology will not be confined to rich countries. Calestous Juma of Harvard University shares Mr Esty's excitement about the possibility of such a technology-driven revolution even in Africa: “In the past, the only environmental ‘database' we had in Africa was our grandmothers. Now, with global information systems and such, the potential is enormous.” Conservationists in Namibia, for example, already use satellite tracking to keep count of their elephants. Farmers in Mali receive satellite updates about impending storms on hand-wound radios. Mr Juma thinks the day is not far off when such technology, combined with ground-based monitoring, will help Africans measure trends in deforestation, soil erosion and climate change, and assess the effects on their local environment.

## Make a start

That is at once a sweeping vision and a modest one. Sweeping, because it will require heavy investment in both sophisticated hardware and nuts-and-bolts information infrastructure on the ground to make sense of all these new data. As the poor world clearly cannot afford to pay for all this, the rich world must help—partly for altruistic reasons, partly with the selfish aim of discovering in good time whether any global environmental calamities are in the making. A number of multilateral agencies now say they are willing to invest in this area as a “neglected global public good”—neglected especially by those agencies themselves. Even President Bush's administration has recently indicated that it will give environmental satellite data free to poor countries.

But that vision is also quite a modest one. Assuming that this data “revolution” does take place, all it will deliver is a reliable assessment of the health of the planet today. We will still not be able to answer the broader question of whether current trends are sustainable or not.

To do that, we need to look more closely at two very different sorts of environmental problems: global crises and local troubles. The global sort is hard to pin down, but can involve irreversible changes. The local kind is common and can have a big effect on the quality of life, but is usually reversible. Data on both are predictably inadequate. We turn first to the most elusive environmental problem of all, global warming.

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# Blowing hot and cold

Jul 4th 2002
From The Economist print edition

**Climate change may be slow and uncertain, but that is no excuse for inaction**

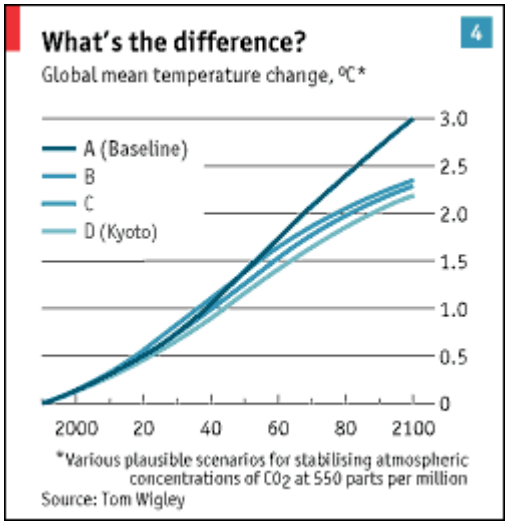
WHAT would Winston Churchill have done about climate change? Imagine that Britain's visionary wartime leader had been presented with a potential time bomb capable of wreaking global havoc, although not certain to do so. Warding it off would require concerted global action and economic sacrifice on the home front. Would he have done nothing?

Not if you put it that way. After all, Churchill did not dismiss the Nazi threat for lack of conclusive evidence of Hitler's evil intentions. But the answer might be less straightforward if the following provisos had been added: evidence of this problem would remain cloudy for decades; the worst effects might not be felt for a century; but the costs of tackling the problem would start biting immediately. That, in a nutshell, is the dilemma of climate change. It is asking a great deal of politicians to take action on behalf of voters who have not even been born yet.

One reason why uncertainty over climate looks to be with us for a long time is that the oceans, which absorb carbon from the atmosphere, act as a time-delay mechanism. Their massive thermal inertia means that the climate system responds only very slowly to changes in the composition of the atmosphere. Another complication arises from the relationship between carbon dioxide ($CO_2$), the principal greenhouse gas (GHG), and sulphur dioxide ($SO_2$), a common pollutant. Efforts to reduce man-made emissions of GHGs by cutting down on fossil-fuel use will reduce emissions of both gases. The reduction in $CO_2$ will cut warming, but the concurrent $SO_2$ cut may mask that effect by contributing to the warming.

There are so many such fuzzy factors—ranging from aerosol particles to clouds to cosmic radiation—that we are likely to see disruptions to familiar climate patterns for many years without knowing why they are happening or what to do about them. Tom Wigley, a leading climate scientist and member of the UN's Intergovernmental Panel on Climate Change (IPCC), goes further. He argues in an excellent book published by the Aspen Institute, “US Policies on Climate Change: What Next?”, that whatever policy changes governments pursue, scientific uncertainties will “make it difficult to detect the effects of such changes, probably for many decades.”

As evidence, he points to the negligible short- to medium-term difference in temperature resulting from an array of emissions “pathways” on which the world could choose to embark if it decided to tackle climate change (see chart 4). He plots various strategies for reducing GHGs (including the Kyoto one) that will lead in the next century to the stabilisation of atmospheric concentrations of $CO_2$ at 550 parts per million (ppm). That is roughly double the level which prevailed in pre-industrial times, and is often mooted by climate scientists as a reasonable target. But even by 2040, the temperature differences between the various options will still be tiny—and certainly within the magnitude of natural climatic variance. In short, in another four decades we will probably still not know if we have over- or undershot.




## Ignorance is not bliss

However, that does not mean we know nothing. We do know, for a start, that the “greenhouse effect” is

real: without the heat-trapping effect of water vapour, $CO_2$, methane and other naturally occurring GHGs, our planet would be a lifeless 30°C or so colder. Some of these GHG emissions are captured and stored by “sinks”, such as the oceans, forests and agricultural land, as part of nature's carbon cycle.

We also know that since the industrial revolution began, mankind's actions have contributed significantly to that greenhouse effect. Atmospheric concentrations of GHGs have risen from around 280ppm two centuries ago to around 370ppm today, thanks chiefly to mankind's use of fossil fuels and, to a lesser degree, to deforestation and other land-use changes. Both surface temperatures and sea levels have been rising for some time.

There are good reasons to think temperatures will continue rising. The IPCC has estimated a likely range for that increase of 1.4°C-5.8°C over the next century, although the lower end of that range is more likely. Since what matters is not just the absolute temperature level but the rate of change as well, it makes sense to try to slow down the increase.

The worry is that a rapid rise in temperatures would lead to climate changes that could be devastating for many (though not all) parts of the world. Central America, most of Africa, much of south Asia and northern China could all be hit by droughts, storms and floods and otherwise made miserable. Because they are poor and have the misfortune to live near the tropics, those most likely to be affected will be least able to adapt.

The colder parts of the world may benefit from warming, but they too face perils. One is the conceivable collapse of the Atlantic “conveyor belt”, a system of currents that gives much of Europe its relatively mild climate; if temperatures climb too high, say scientists, the system may undergo radical changes that damage both Europe and America. That points to the biggest fear: warming may trigger irreversible changes that transform the earth into a largely uninhabitable environment.

Given that possibility, extremely remote though it is, it is no comfort to know that any attempts to stabilise atmospheric concentrations of GHGs at a particular level will take a very long time. Because of the oceans' thermal inertia, explains Mr Wigley, even once atmospheric concentrations of GHGs are stabilised, it will take decades or centuries for the climate to follow suit. And even then the sea level will continue to rise, perhaps for millennia.

This is a vast challenge, and it is worth bearing in mind that mankind's contribution to warming is the only factor that can be controlled. So the sooner we start drawing up a long-term strategy for climate change, the better.

What should such a grand plan look like? First and foremost, it must be global. Since $CO_2$ lingers in the atmosphere for a century or more, any plan must also extend across several generations.

The plan must recognise, too, that climate change is nothing new: the climate has fluctuated through history, and mankind has adapted to those changes—and must continue doing so. In the rich world, some of the more obvious measures will include building bigger dykes and flood defences. But since the most vulnerable people are those in poor countries, they too have to be helped to adapt to rising seas and unpredictable storms. Infrastructure improvements will be useful, but the best investment will probably be to help the developing world get wealthier.

It is essential to be clear about the plan's long-term objective. A growing chorus of scientists now argues that we need to keep temperatures from rising by much more than 2-3°C in all. That will require the stabilisation of atmospheric concentrations of GHGs. James Edmonds of the University of Maryland points out that because of the long life of $CO_2$, stabilisation of $CO_2$ concentrations is not at all the same thing as stabilisation of $CO_2$ emissions. That, says Mr Edmonds, points to an unavoidable conclusion: “In the very long term, global net $CO_2$ emissions must eventually peak and gradually decline toward zero, regardless of whether we go for a target of 350ppm or 1,000ppm.”

## A low-carbon world

That is why the long-term objective for climate policy must be a transition to a low-carbon energy system. Such a transition can be very gradual and need not necessarily lead to a world powered only by bicycles and windmills, for two reasons that are often overlooked.

One involves the precise form in which the carbon in the ground is distributed. According to Michael Grubb of the Carbon Trust, a British quasi-governmental body, the long-term problem is coal. In theory, we can burn all of the conventional oil and natural gas in the ground and still meet the most ambitious goals for tackling climate change. If we do that, we must ensure that the far greater amounts of carbon trapped as coal (and unconventional resources like tar sands) never enter the atmosphere.

The snag is that poor countries are likely to continue burning cheap domestic reserves of coal for decades. That suggests the rich world should speed the development and diffusion of "low carbon" technologies using the energy content of coal without releasing its carbon into the atmosphere. This could be far off, so it still makes sense to keep a watchful eye on the soaring carbon emissions from oil and gas.

The other reason, as Mr Edmonds took care to point out, is that it is net emissions of $CO_2$ that need to peak and decline. That leaves scope for the continued use of fossil fuels as the main source of modern energy if only some magical way can be found to capture and dispose of the associated $CO_2$. Happily, scientists already have some magic in the works.

One option is the biological "sequestration" of carbon in forests and agricultural land. Another promising idea is capturing and storing $CO_2$—underground, as a solid or even at the bottom of the ocean. Planting "energy crops" such as switch-grass and using them in conjunction with sequestration techniques could even result in negative net $CO_2$ emissions, because such plants use carbon from the atmosphere. If sequestration is combined with techniques for stripping the hydrogen out of this hydrocarbon, then coal could even offer a way to sustainable hydrogen energy.

But is anyone going to pay attention to these long-term principles? After all, over the past couple of years all participants in the Kyoto debate have excelled at producing short-sighted, selfish and disingenuous arguments. And the political rift continues: the EU and Japan pushed ahead with ratification of the Kyoto treaty a month ago, whereas President Bush reaffirmed his opposition.

However, go back a decade and you will find precisely those principles enshrined in a treaty approved by the elder George Bush and since reaffirmed by his son: the UN Framework Convention on Climate Change (FCCC). This treaty was perhaps the most important outcome of the Rio summit, and it remains the basis for the international climate-policy regime, including Kyoto.

The treaty is global in nature and long-term in perspective. It commits signatories to pursuing "the stabilisation of GHG concentrations in the atmosphere at a level that would prevent dangerous interference with the climate system." Note that the agreement covers GHG concentrations, not merely emissions. In effect, this commits even gas-guzzling America to the goal of declining emissions.

## Better than Kyoto

Crucially, the FCCC treaty not only lays down the ends but also specifies the means: any strategy to achieve stabilisation of GHG concentrations, it insists, "must not be disruptive of the global economy". That was the stumbling block for the Kyoto treaty, which is built upon the FCCC agreement: its targets and timetables proved unrealistic.

Any revised Kyoto treaty or follow-up accord (which must include the United States and the big developing countries) should rest on three basic pillars. First, governments everywhere (but especially in Europe) must understand that a reduction in emissions has to start modestly. That is because the capital stock involved in the global energy system is vast and long-lived, so a dash to scrap fossil-fuel production would be hugely expensive. However, as Mr Grubb points out, that pragmatism must be flanked by policies that encourage a switch to low-carbon technologies when replacing existing plants.

Second, governments everywhere (but especially in America) must send a powerful signal that carbon is going out of fashion. The best way to do this is to levy a carbon tax. However, whether it is done through taxes, mandated restrictions on GHG emissions or market mechanisms is less important than that the signal is sent clearly, forcefully and unambiguously. This is where President Bush's mixed signals have done a lot of harm: America's industry, unlike Europe's, has little incentive to invest in low-carbon technology. The irony is that even some coal-fired utilities in America are now clamouring for $CO_2$ regulation so that they can invest in new plants with confidence.

The third pillar is to promote science and technology. That means encouraging basic climate and energy research, and giving incentives for spreading the results. Rich countries and aid agencies must also find ways to help the poor world adapt to climate change. This is especially important if the world starts off with small cuts in emissions, leaving deeper cuts for later. That, observes Mr Wigley, means that by mid-century “very large investments would have to have been made—and yet the ‘return' on these investments would not be visible. Continued investment is going to require more faith in climate science than currently appears to be the case.”

Even a visionary like Churchill might have lost heart in the face of all this uncertainty. Nevertheless, there is a glimmer of hope that today's peacetime politicians may rise to the occasion.

## Miracles sometimes happen

Two decades ago, the world faced a similar dilemma: evidence of a hole in the ozone layer. Some inconclusive signs suggested that it was man-made, caused by the use of chlorofluorocarbons (CFCs). There was the distant threat of disaster, and the knowledge that a concerted global response was required. Industry was reluctant at first, yet with leadership from Britain and America the Montreal Protocol was signed in 1987. That deal has proved surprisingly successful. The manufacture of CFCs is nearly phased out, and there are already signs that the ozone layer is on the way to recovery.

This story holds several lessons for the admittedly far more complex climate problem. First, it is the rich world which has caused the problem and which must lead the way in solving it. Second, the poor world must agree to help, but is right to insist on being given time—as well as money and technology—to help it adjust. Third, industry holds the key: in the ozone-depletion story, it was only after DuPont and ICI broke ranks with the rest of the CFC manufacturers that a deal became possible. On the climate issue, BP and Shell have similarly broken ranks with Big Oil, but the American energy industry—especially the coal sector—remains hostile.

The final lesson is the most important: that the uncertainty surrounding a threat such as climate change is no excuse for inaction. New scientific evidence shows that the threat from ozone depletion had been much deadlier than was thought at the time when the world decided to act. Churchill would surely have approved.

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# Local difficulties

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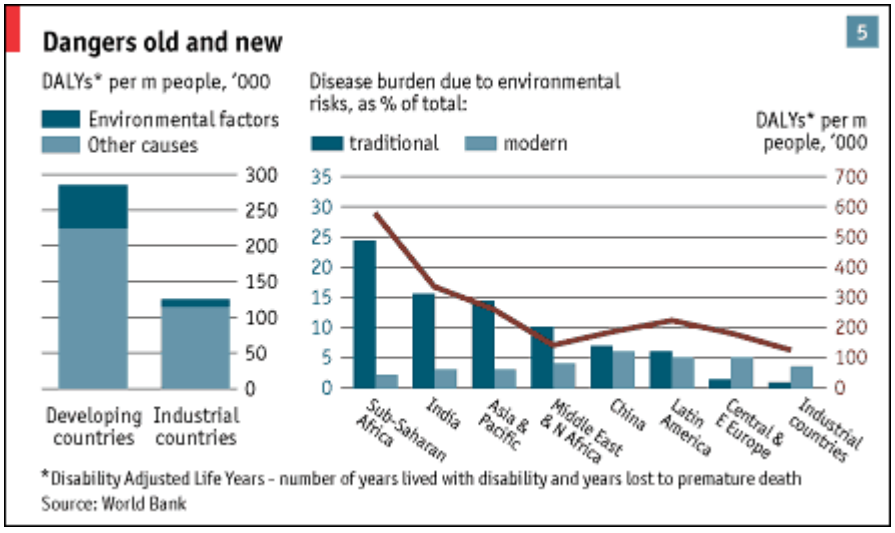
**Greenery is for the poor too, particularly on their own doorstep**

WHY should we care about the environment? Ask a European, and he will probably point to global warming. Ask the two little boys playing outside a newsstand in Da Shilan, a shabby neighbourhood in the heart of Beijing, and they will tell you about the city's notoriously foul air: “It's bad—like a virus!”

Given all the media coverage in the rich world, people there might believe that global scares are the chief environmental problems facing humanity today. They would be wrong. Partha Dasgupta, an economics professor at Cambridge University, thinks the current interest in global, future-oriented problems has “drawn attention away from the economic misery and ecological degradation endemic in large parts of the world today. Disaster is not something for which the poorest have to wait; it is a frequent occurrence.”

Every year in developing countries, a million people die from urban air pollution and twice that number from exposure to stove smoke inside their homes. Another 3m unfortunates die prematurely every year from water-related diseases. All told, premature deaths and illnesses arising from environmental factors account for about a fifth of all diseases in poor countries, bigger than any other preventable factor, including malnutrition. The problem is so serious that Ian Johnson, the World Bank's vice-president for the environment, tells his colleagues, with a touch of irony, that he is really the bank's vice-president for health: “I say tackling the underlying environmental causes of health problems will do a lot more good than just more hospitals and drugs.”

The link between environment and poverty is central to that great race for sustainability. It is a pity, then, that several powerful fallacies keep getting in the way of sensible debate. One popular myth is that trade and economic growth make poor countries' environmental problems worse. Growth, it is said, brings with it urbanisation, higher energy consumption and industrialisation—all factors that contribute to pollution and pose health risks.




In a static world, that would be true, because every new factory causes extra pollution. But in the real world, economic growth unleashes many dynamic forces that, in the longer run, more than offset that extra pollution. As chart 5 makes clear, traditional environmental risks (such as water-borne diseases) cause far more health problems in poor countries than modern environmental risks (such as industrial pollution).

## Rigged rules

However, this is not to say that trade and economic growth will solve all environmental problems. Among the reasons for doubt are the “perverse” conditions under which world trade is carried on, argues Oxfam. The British charity thinks the rules of trade are “unfairly rigged against the poor”, and cites in evidence the enormous subsidies lavished by rich countries on industries such as agriculture, as well as trade protection offered to manufacturing industries such as textiles. These measures hurt the environment because they force the world's poorest countries to rely heavily on commodities—a particularly energy-intensive and ungreen sector.

Mr Dasgupta argues that this distortion of trade amounts to a massive subsidy of rich-world consumption paid by the world's poorest people. The most persuasive critique of all goes as follows: “Economic growth is not sufficient for turning environmental degradation around. If economic incentives facing producers and consumers do not change with higher incomes, pollution will continue to grow unabated with the growing scale of economic activity.” Those words come not from some anti-globalist green group, but from the World Trade Organisation.

Another common view is that poor countries, being unable to afford greenery, should pollute now and clean up later. Certainly poor countries should not be made to adopt American or European environmental standards. But there is evidence to suggest that poor countries can and should try to tackle some environmental problems now, rather than wait till they have become richer.

This so-called “smart growth” strategy contradicts conventional wisdom. For many years, economists have observed that as agrarian societies industrialised, pollution increased at first, but as the societies grew wealthier it declined again. The trouble is that this applies only to some pollutants, such as sulphur dioxide, but not to others, such as carbon dioxide. Even more troublesome, those smooth curves going up, then down, turn out to be misleading. They are what you get when you plot data for poor and rich countries together at a given moment in time, but actual levels of various pollutants in any individual country plotted over time wiggle around a lot more. This suggests that the familiar bell-shaped curve reflects no immutable law, and that intelligent government policies might well help to reduce pollution levels even while countries are still relatively poor.

Developing countries are getting the message. From Mexico to the Philippines, they are now trying to curb the worst of the air and water pollution that typically accompanies industrialisation. China, for example, was persuaded by outside experts that it was losing so much potential economic output through health troubles caused by pollution (according to one World Bank study, somewhere between 3.5% and 7.7% of GDP) that tackling it was cheaper than ignoring it.

One powerful—and until recently ignored—weapon in the fight for a better environment is local people. Old-fashioned paternalists in the capitals of developing countries used to argue that poor villagers could not be relied on to look after natural resources. In fact, much academic research has shown that the poor are more often victims than perpetrators of resource depletion: it tends to be rich locals or outsiders who are responsible for the worst exploitation.

Local people usually have a better knowledge of local ecological conditions than experts in faraway capitals, as well as a direct interest in improving the quality of life in their village. A good example of this comes from the bone-dry state of Rajasthan in India, where local activism and indigenous know-how about rainwater “harvesting” provided the people with reliable water supplies—something the government had failed to do. In Bangladesh, villages with active community groups or concerned mullahs proved greener than less active neighbouring villages.

Community-based forestry initiatives from Bolivia to Nepal have shown that local people can be good custodians of nature. Several hundred million of the world's poorest people live in and around forests. Giving those villagers an incentive to preserve forests by allowing sustainable levels of harvesting, it turns out, is a far better way to save those forests than erecting tall fences around them.

To harness local energies effectively, it is particularly important to give local people secure property rights, argues Mr Dasgupta. In most parts of the developing world, control over resources at the village level is ill-defined. This often means that local elites usurp a disproportionate share of those resources, and that individuals have little incentive to maintain and upgrade forests or agricultural land. Authorities in Thailand tried to remedy this problem by distributing 5.5m land titles over a 20-year period. Agricultural output increased, access to credit improved and the value of the land shot up.

## Name and shame

Another powerful tool for improving the local environment is the free flow of information. As local democracy flourishes, ordinary people are pressing for greater environmental disclosure by companies. In some countries, such as Indonesia, governments have adopted a “sunshine” policy that involves naming and shaming companies that do not meet environmental regulations. It seems to achieve results.

Bringing greenery to the grass roots is good, but on its own it will not avert perceived threats to global “public goods” such as the climate or biodiversity. Paul Portney of Resources for the Future explains: “Brazilian villagers may think very carefully and unselfishly about their future descendants, but there's no reason for them to care about and protect species or habitats that no future generation of Brazilians will care about.”

That is why rich countries must do more than make pious noises about global threats to the environment. If they believe that scientific evidence suggests a credible threat, they must be willing to pay poor countries to protect such things as their tropical forests. Rather than thinking of this as charity, they should see it as payment for environmental services (say, for carbon storage) or as a form of insurance.

In the case of biodiversity, such payments could even be seen as a trade in luxury goods: rich countries would pay poor countries to look after creatures that only the rich care about. Indeed, private green groups are already buying up biodiversity “hot spots” to protect them. One such initiative, led by Conservation International and the International Union for the Conservation of Nature (IUCN), put the cost of buying and preserving 25 hot spots exceptionally rich in species diversity at less than $30 billion. Sceptics say it will cost more, as hot spots will need buffer zones of “sustainable harvesting” around them. Whatever the right figure, such creative approaches are more likely to achieve results than bullying the poor into conservation.

It is not that the poor do not have green concerns, but that those concerns are very different from those of the rich. In Beijing's Da Shilan, for instance, the air is full of soot from the many tiny coal boilers. Unlike most of the neighbouring districts, which have recently converted from coal to natural gas, this area has been considered too poor to make the transition. Yet ask Liu Shihua, a shopkeeper who has lived in the same spot for over 20 years, and he insists he would readily pay a bit more for the cleaner air that would come from using natural gas. So would his neighbours.

To discover the best reason why poor countries should not ignore pollution, ask those two little boys outside Mr Liu's shop what colour the sky is. “Grey!” says one tyke, as if it were the most obvious thing in the world. “No, stupid, it's blue!” retorts the other. The children deserve blue skies and clean air. And now there is reason to think they will see them in their lifetime.

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# Working miracles

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**Can technology save the planet?**

“NOTHING endures but change.” That observation by Heraclitus often seems lost on modern environmental thinkers. Many invoke scary scenarios assuming that resources—both natural ones, like oil, and man-made ones, like knowledge—are fixed. Yet in real life man and nature are entwined in a dynamic dance of development, scarcity, degradation, innovation and substitution.

The nightmare about China turning into a resource-guzzling America raises two questions: will the world run out of resources? And even if it does not, could the growing affluence of developing nations lead to global environmental disaster?

The first fear is the easier to refute; indeed, history has done so time and again. Malthus, Ricardo and Mill all worried that scarcity of resources would snuff out growth. It did not. A few decades ago, the limits-to-growth camp raised worries that the world might soon run out of oil, and that it might not be able to feed the world's exploding population. Yet there are now more proven reserves of petroleum than three decades ago; there is more food produced than ever; and the past decade has seen history's greatest economic boom.

What made these miracles possible? Fears of oil scarcity prompted investment that led to better ways of producing oil, and to more efficient engines. In food production, technological advances have sharply reduced the amount of land required to feed a person in the past 50 years. Jesse Ausubel of Rockefeller University calculates that if in the next 60 to 70 years the world's average farmer reaches the yield of today's average (not best) American maize grower, then feeding 10 billion people will require just half of today's cropland. All farmers need to do is maintain the 2%-a-year productivity gain that has been the global norm since 1960.

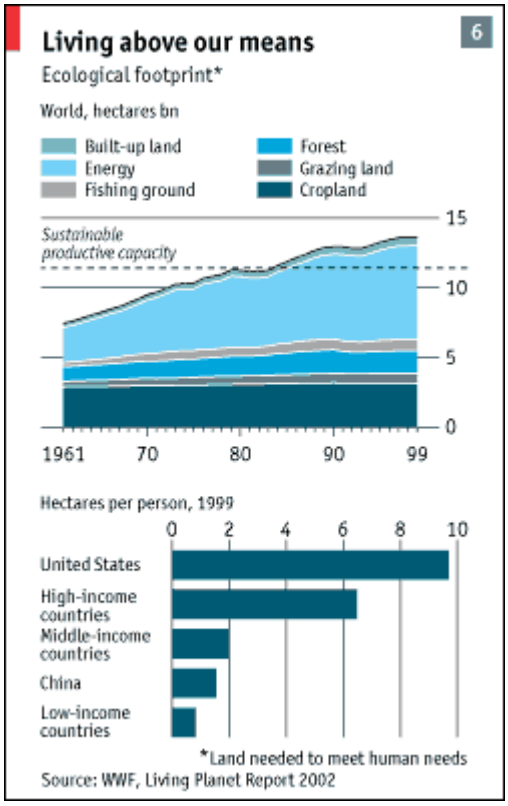
“Scarcity and Growth”, a book published by Resources for the Future, sums it up brilliantly: “Decades ago Vermont granite was only building and tombstone material; now it is a potential fuel, each ton of which has a usable energy content (uranium) equal to 150 tons of coal. The notion of an absolute limit to natural resource availability is untenable when the definition of resources changes drastically and unpredictably over time.” Those words were written by Harold Barnett and Chandler Morse in 1963, long before the limits-to-growth bandwagon got rolling.

## Giant footprint

Not so fast, argue greens. Even if we are not going to run out of resources, guzzling ever more resources could still do irreversible damage to fragile ecosystems.

WWF, an environmental group, regularly calculates mankind's “ecological footprint”, which it defines as the “biologically productive land and water areas required to produce the resources consumed and assimilate the wastes generated by a given population using prevailing technology.” The group reckons the planet has around 11.4 billion “biologically productive” hectares of land available to meet continuing human needs. As chart 6 shows, WWF thinks mankind has recently been using more than that. This is possible because a forest harvested at twice its regeneration rate, for example, appears in the footprint accounts at twice its area—an unsustainable practice which the group calls “ecological overshoot”.

Any analysis of this sort must be viewed with scepticism. Everyone knows that environmental data are incomplete. What is more, the biggest factor by far is the land required to absorb $CO_2$ emissions of fossil fuels. If that problem could be managed some other way, then mankind's ecological footprint would look much more sustainable.




Even so, the WWF analysis makes an important point: if China's economy were transformed overnight into a clone of America's, an ecological nightmare could ensue. If a billion eager new consumers were suddenly to produce $CO_2$emissions at American rates, they would be bound to accelerate global warming. And if the whole of the developing world were to adopt an American lifestyle tomorrow, local environmental crises such as desertification, aquifer depletion and topsoil loss could make humans miserable.

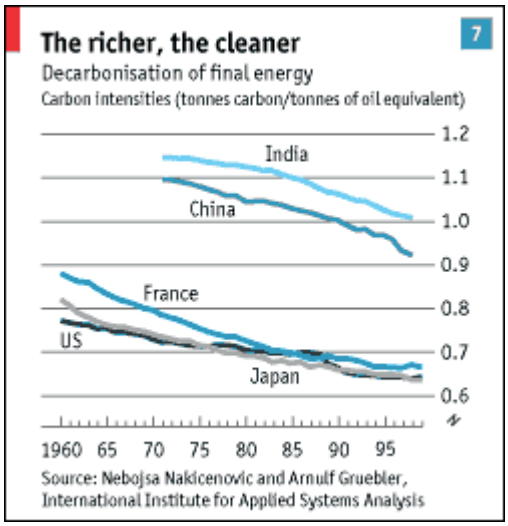
So is this cause for concern? Yes, but not for panic. The global ecological footprint is determined by three factors: population size, average consumption per person and technology. Fortunately, global population growth now appears to be moderating. Consumption per person in poor countries is rising as they become better off, but there are signs that the rich world is reducing the footprint of its consumption(as this survey's final section explains). The most powerful reason for hope—innovation—was foreshadowed by WWF's own definition. Today's “prevailing technologies” will, in time, be displaced by tomorrow's greener ones.

“The rest of the world will not live like America,” insists Mr Ausubel. Of course poor people around the world covet the creature comforts that Americans enjoy, but they know full well that the economic growth needed to improve their lot will take time. Ask Wu Chengjian, an environmental official in booming Shanghai, what he thinks of the popular notion that his city might become as rich as today's Hong Kong by 2020: “Impossible—that's just not enough time.” And that is Shanghai, not the impoverished countryside.

## Leaps of faith

This extra time will allow poor countries to embrace new technologies that are more efficient and less environmentally damaging. That still does not guarantee a smaller ecological footprint for China in a few decades' time than for America now, but it greatly improves the chances. To see why, consider the history of “dematerialisation” and “decarbonisation” (see chart 7). Viewed across very long spans of time, productivity improvements allow economies to use ever fewer material inputs—and to emit ever fewer pollutants—per unit of economic output. Mr Ausubel concludes: “When China has today's American mobility, it will not have today's American cars,” but the cleaner and more efficient cars of tomorrow.

The snag is that consumers in developing countries want to drive cars not tomorrow but today. The resulting emissions have led many to despair that technology (in the form of vehicles) is making matters worse, not better.




Can they really hope to “leapfrog” ahead to cleaner air? The evidence from Los Angeles—a pioneer in the fight against air pollution—suggests the answer is yes. “When I moved to Los Angeles in the 1960s, there was so much soot in the air that it felt like there was a man standing on your chest most of the time,” says Ron Loveridge, the mayor of Riverside, a city to the east of LA that suffers the worst of the region's pollution. But, he says, “We have come an extraordinary distance in LA.”

Four decades ago, the city had the worst air quality in America. The main problem was the city's infamous “smog” (an amalgam of “smoke” and “fog”). It took a while to figure out that this

unhealthy ozone soup developed as a result of complex chemical reactions between nitrogen oxides and volatile organic compounds that need sunlight to trigger them off.

Arthur Winer, an atmospheric chemist at the University of California at Los Angeles, explains that tackling smog required tremendous perseverance and political will. Early regulatory efforts met stiff resistance from business interests, and began to falter when they failed to show dramatic results.

Clean-air advocates like Mr Loveridge began to despair: “We used to say that we needed a ‘London fog' [a reference to an air-pollution episode in 1952 that may have killed 12,000 people in that city] here to force change.” Even so, Californian officials forged ahead with an ambitious plan that combined regional regulation with stiff mandates for cleaner air. Despite uncertainties about the cause of the problem, the authorities introduced a sequence of controversial measures: unleaded and low-sulphur petrol, on-board diagnostics for cars to minimise emissions, three-way catalytic converters, vapour-recovery attachments for petrol nozzles and so on.

As a result, the city that two decades ago hardly ever met federal ozone standards has not had to issue a single alert in the past three years. Peak ozone levels are down by 50% since the 1960s. Though the population has shot up in recent years, and the vehicle-miles driven by car-crazy Angelenos have tripled, ozone levels have fallen by two-thirds. The city's air is much cleaner than it was two decades ago.

“California, in solving its air-quality problem, has solved it for the rest of the United States and the world—but it doesn't get credit for it,” says Joe Norbeck of the University of California at Riverside. He is adamant that the poor world's cities can indeed leapfrog ahead by embracing some of the cleaner technologies developed specifically for the Californian market. He points to China's vehicle fleet as an example: “China's typical car has the emissions of a 1974 Ford Pinto, but the new Buicks sold there use 1990s emissions technology.” The typical car sold today produces less than a tenth of the local pollution of a comparable model from the 1970s.

That suggests one lesson for poor cities such as Beijing that are keen to clean up: they can order polluters to meet high emissions standards. Indeed, from Beijing to Mexico city, regulators are now imposing rich-world rules, mandating new, cleaner technologies. In China's cities, where pollution from sooty coal fires in homes and industrial boilers had been a particular hazard, officials are keen to switch to natural-gas furnaces.

However, there are several reasons why such mandates—which worked wonders in LA—may be trickier to achieve in impoverished or politically weak cities. For a start, city officials must be willing to pay the political price of reforms that raise prices for voters. Besides, higher standards for new cars, useful though they are, cannot do the trick on their own. Often, clean technologies such as catalytic converters will require cleaner grades of petrol too. Introducing cleaner fuels, say experts, is an essential lesson from LA for poor countries. This will not come free either.

There is another reason why merely ordering cleaner new cars is inadequate: it does nothing about the vast stock of dirty old ones already on the streets. In most cities of the developing world, the oldest fifth of the vehicles on the road is likely to produce over half of the total pollution caused by all vehicles taken together. Policies that encourage a speedier turnover of the fleet therefore make more sense than “zero emissions” mandates.

## Policy matters

In sum, there is hope that the poor can leapfrog at least some environmental problems, but they need more than just technology. Luisa and Mario Molina of the Massachusetts Institute of Technology, who have studied such questions closely, reckon that technology is less important than the institutional capacity, legal safeguards and financial resources to back it up: “The most important underlying factor is political will.” And even a techno-optimist such as Mr Ausubel accepts that: “There is nothing automatic about technological innovation and adoption; in fact, at the micro level, it's bloody.”

Clearly innovation is a powerful force, but government policy still matters. That suggests two rules for policymakers. First, don't do stupid things that inhibit innovation. Second, do sensible things that reward the development and adoption of technologies that enhance, rather than degrade, the environment.

The greatest threat to sustainability may well be the rejection of science. Consider Britain's hysterical reaction to genetically modified crops, and the European Commission's recent embrace of a woolly

“precautionary principle”. Precaution applied case-by-case is a undoubtedly a good thing, but applying any such principle across the board could prove disastrous.

Explaining how not to stifle innovation that could help the environment is a lot easier than finding ways to encourage it. Technological change often goes hand-in-hand with greenery by saving resources, as the long history of dematerialisation shows—but not always. Sports utility vehicles, for instance, are technologically innovative, but hardly green. Yet if those SUVs were to come with hydrogen-powered fuel cells that emit little pollution, the picture would be transformed.

The best way to encourage such green innovations is to send powerful signals to the market that the environment matters. And there is no more powerful signal than price, as the next section explains.

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# The invisible green hand

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**Markets could be a potent force for greenery—if only greens could learn to love them**

“MANDATE, regulate and litigate.” That has been the environmentalists' rallying cry for ages. Nowhere in the green manifesto has there been much mention of the market. And, oddly, it was market-minded America that led the dirigiste trend. Three decades ago, Congress passed a sequence of laws, including the Clean Air Act, which set lofty goals and generally set rigid technological standards. Much of the world followed America's lead.

This top-down approach to greenery has long been a point of pride for groups such as the Natural Resources Defence Council (NRDC), one of America's most influential environmental outfits. And with some reason, for it has had its successes: the air and water in the developed world is undoubtedly cleaner than it was three decades ago, even though the rich world's economies have grown by leaps and bounds. This has convinced such groups stoutly to defend the green status quo.

But times may be changing. Gus Speth, now head of Yale University's environment school and formerly head of the World Resources Institute and the UNDP, as well as one of the founders of the NRDC, recently explained how he was converted to market economics: “Thirty years ago, the economists at Resources for the Future were pushing the idea of pollution taxes. We lawyers at NRDC thought they were nuts, and feared that they would derail command-and-control measures like the Clean Air Act, so we opposed them. Looking back, I'd have to say this was the single biggest failure in environmental management—not getting the prices right.”

A remarkable mea culpa; but in truth, the command-and-control approach was never as successful as its advocates claimed. For example, although it has cleaned up the air and water in rich countries, it has notably failed in dealing with waste management, hazardous emissions and fisheries depletion. Also, the gains achieved have come at a needlessly high price. That is because technology mandates and bureaucratic edicts stifle innovation and ignore local realities, such as varying costs of abatement. They also fail to use cost-benefit analysis to judge trade-offs.

Command-and-control methods will also be ill-suited to the problems of the future, which are getting trickier. One reason is that the obvious issues—like dirty air and water—have been tackled already. Another is increasing technological complexity: future problems are more likely to involve subtle linkages—like those involved in ozone depletion and global warming—that will require sophisticated responses. The most important factor may be society's ever-rising expectations: as countries grow wealthier, their people start clamouring for an ever-cleaner environment. But because the cheap and simple things have been done, that is proving increasingly expensive. Hence the greens' new interest in the market.

## Carrots, not just sticks

In recent years, market-based greenery has taken off in several ways. With emissions trading, officials decide on a pollution target and then allocate tradable credits to companies based on that target. Those that find it expensive to cut emissions can buy credits from those that find it cheaper, so the target is achieved at the minimum cost and disruption.

The greatest green success story of the past decade is probably America's innovative scheme to cut emissions of sulphur dioxide ($SO_2$). Dan Dudek of Environmental Defence, a most unusual green group, and his market-minded colleagues persuaded the elder George Bush to agree to an amendment to the sacred Clean Air Act that would introduce an emissions-trading system to achieve sharp cuts in $SO_2$. At the time, this was hugely controversial: America's power industry insisted the cuts were prohibitively

costly, while nearly every other green group decried the measure as a sham. In the event, ED has been vindicated. America's scheme has surpassed its initial objectives, and at far lower cost than expected. So great is the interest worldwide in trading that ED is now advising groups ranging from hard-nosed oilmen at BP to bureaucrats in China and Russia.

Europe, meanwhile, is forging ahead with another sort of market-based instrument: pollution taxes. The idea is to levy charges on goods and services so that their price reflects their “externalities”—jargon for how much harm they do to the environment and human health. Sweden introduced a sulphur tax a decade ago, and found that the sulphur content of fuels dropped 50% below legal requirements.

Though “tax” still remains a dirty word in America, other parts of the world are beginning to embrace green tax reform by shifting taxes from employment to pollution. Robert Williams of Princeton University has looked at energy use (especially the terrible effects on health of particulate pollution) and concluded that such externalities are comparable in size to the direct economic costs of producing that energy.

Externalities are only half the battle in fixing market distortions. The other half involves scrapping environmentally harmful subsidies. These range from prices below market levels for electricity and water to shameless cash handouts for industries such as coal. The boffins at the OECD reckon that stripping away harmful subsidies, along with introducing taxes on carbon-based fuels and chemicals use, would result in dramatically lower emissions by 2020 than current policies would be able to achieve. If the revenues raised were then used to reduce other taxes, the cost of these virtuous policies would be less than 1% of the OECD's economic output in 2020.

Such subsidies are nothing short of perverse, in the words of Norman Myers of Oxford University. They do double damage, by distorting markets and by encouraging behaviour that harms the environment. Development banks say such subsidies add up to $700 billion a year, but Mr Myers reckons the true sum is closer to $2 trillion a year. Moreover, the numbers do not fully reflect the harm done. For example, EU countries subsidise their fishing fleets to the tune of $1 billion a year, but that has encouraged enough overfishing to drive many North Atlantic fishing grounds to near-collapse.

Fishing is an example of the “tragedy of the commons”, which pops up frequently in the environmental debate. A resource such as the ocean is common to many, but an individual “free rider” can benefit from plundering that commons or dumping waste into it, knowing that the costs of his actions will probably be distributed among many neighbours. In the case of shared fishing grounds, the absence of individual ownership drives each fisherman to snatch as many fish as he can—to the detriment of all.

## Of rights and wrongs

Assigning property rights can help, because providing secure rights (set at a sustainable level) aligns the interests of the individual with the wider good of preserving nature. This is what sceptical conservationists have observed in New Zealand and Iceland, where schemes for tradable quotas have helped revive fishing stocks. Similar rights-based approaches have led to revivals in stocks of African elephants in southern Africa, for example, where the authorities stress property rights and private conservation.

All this talk of property rights and markets makes many mainstream environmentalists nervous. Carl Pope, the boss of the Sierra Club, one of America's biggest green groups, does not reject market forces out of hand, but expresses deep scepticism about their scope. Pointing to the difficult problem of climate change, he asks: “Who has property rights over the commons?”

Even so, some greens have become converts. Achim Steiner of the IUCN reckons that the only way forward is rights-based conservation, allowing poor people “sustainable use” of their local environment. Paul Faeth of the World Resources Institute goes further. He says he is convinced that market forces could deliver that holy grail of environmentalism, sustainability—“but only if we get prices right.”

## The limits to markets

Economic liberals argue that the market itself is the greatest price-discovery mechanism known to man. Allow it to function freely and without government meddling, goes the argument, and prices are discovered and internalised automatically. Jerry Taylor of the Cato Institute, a libertarian think-tank,

insists that “The world today is already sustainable—except those parts where western capitalism doesn't exist.” He notes that countries that have relied on central planning, such as the Soviet Union, China and India, have invariably misallocated investment, stifled innovation and fouled their environment far more than the prosperous market economies of the world have done.

All true. Even so, markets are currently not very good at valuing environmental goods. Noble attempts are under way to help them do better. For example, the Katoomba Group, a collection of financial and energy companies that have linked up with environmental outfits, is trying to speed the development of markets for some of forestry's ignored “co-benefits” such as carbon storage and watershed management, thereby producing new revenue flows for forest owners. This approach shows promise: water consumers ranging from officials in New York city to private hydro-electric operators in Costa Rica are now paying people upstream to manage their forests and agricultural land better. Paying for greenery upstream turns out to be cheaper than cleaning up water downstream after it has been fouled.

Economists too are getting into the game of helping capitalism “get prices right.” The World Bank's Ian Johnson argues that conventional economic measures such as gross domestic product are not measuring wealth creation properly because they ignore the effects of environmental degradation. He points to the positive contribution to China's GDP from the logging industry, arguing that such a calculation completely ignores the billions of dollars-worth of damage from devastating floods caused by over-logging. He advocates a more comprehensive measure the Bank is working on, dubbed “genuine GDP”, that tries (imperfectly, he accepts) to measure depletion of natural resources.

That could make a dramatic difference to how the welfare of the poor is assessed. Using conventional market measures, nearly the whole of the developing world save Africa has grown wealthier in the past couple of decades. But when the degradation of nature is properly accounted for, argues Mr Dasgupta at Cambridge, the countries of Africa and south Asia are actually much worse off today than they were a few decades ago—and even China, whose economic “miracle” has been much trumpeted, comes out barely ahead.

The explanation, he reckons, lies in a particularly perverse form of market distortion: “Countries that are exporting resource-based products (often among the poorest) may be subsidising the consumption of countries that are doing the importing (often among the richest).” As evidence, he points to the common practice in poor countries of encouraging resource extraction. Whether through licences granted at below-market rates, heavily subsidised exports or corrupt officials tolerating illegal exploitation, he reckons the result is the same: “The cruel paradox we face may well be that contemporary economic development is unsustainable in poor countries because it is sustainable in rich countries.”

One does not have to agree with Mr Dasgupta's conclusion to acknowledge that markets have their limits. That should not dissuade the world from attempting to get prices right—or at least to stop getting them so wrong. For grotesque subsidies, the direction of change should be obvious. In other areas, the market itself may not provide enough information to value nature adequately. This is true of threats to essential assets, such as nature's ability to absorb and “recycle” $CO_2$, that have no substitute at any price. That is when governments must step in, ensuring that an informed public debate takes place.

Robert Stavins of Harvard University argues that the thorny notion of sustainable development can be reduced to two simple ideas: efficiency and intergenerational equity. The first is about making the economic pie as large as possible; he reckons that economists are well equipped to handle it, and that market-based policies can be used to achieve it. On the second (the subject of the next section), he is convinced that markets must yield to public discourse and government policy: “Markets can be efficient, but nobody ever said they're fair. The question is, what do we owe the future?”

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# Insuring a brighter future

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**How to hedge against tomorrow's environmental risks**

SO WHAT do we owe the future? A precise definition for sustainable development is likely to remain elusive but, as this survey has argued, the hazy outline of a useful one is emerging from the experience of the past decade.

For a start, we cannot hope to turn back the clock and return nature to a pristine state. Nor must we freeze nature in the state it is today, for that gift to the future would impose an unacceptable burden on the poorest alive today. Besides, we cannot forecast the tastes, demands or concerns of future generations. Recall that the overwhelming pollution problem a century ago was horse manure clogging up city streets: a century hence, many of today's problems will surely seem equally irrelevant. We should therefore think of our debt to the future as including not just natural resources but also technology, institutions and especially the capacity to innovate. Robert Solow got it mostly right a decade ago: the most important thing to leave future generations, he said, is the capacity to live as well as we do today.

However, as the past decade has made clear, there is a limit to that argument. If we really care about the “sustainable” part of sustainable development, we must be much more watchful about environmental problems with critical thresholds. Most local problems are reversible and hence no cause for alarm. Not all, however: the depletion of aquifers and the loss of topsoil could trigger irreversible changes that would leave future generations worse off. And global or long-term threats, where victims are far removed in time and space, are easy to brush aside.

In areas such as biodiversity, where there is little evidence of a sustainability problem, a voluntary approach is best. Those in the rich world who wish to preserve pandas, or hunt for miracle drugs in the rainforest, should pay for their predilections. However, where there are strong scientific indications of unsustainability, we must act on behalf of the future—even at the price of today's development. That may be expensive, so it is prudent to try to minimise those risks in the first place.

## A riskier world

Human ingenuity and a bit of luck have helped mankind stay a few steps ahead of the forces degrading the environment this past century, the first full one in which the planet has been exposed to industrialisation. In the century ahead, the great race between development and degradation could well become a closer call.

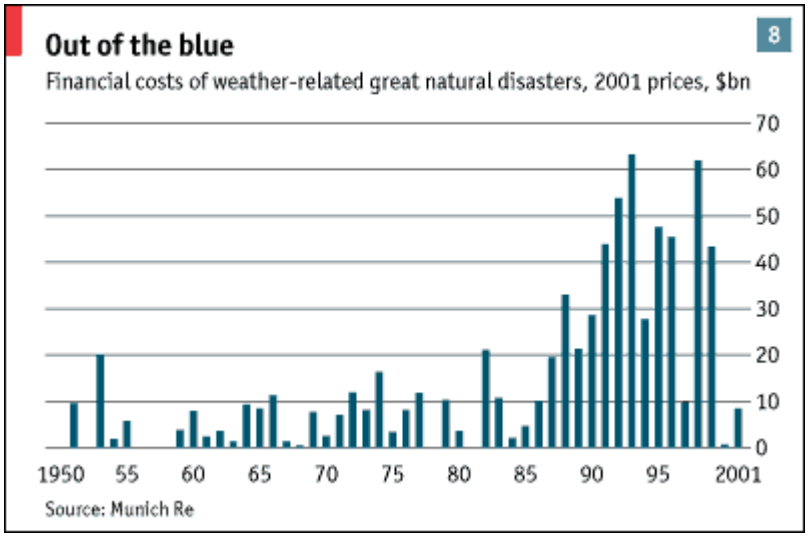
On one hand, the demands of development seem sure to grow at a cracking pace in the next few decades as the Chinas, Indias and Brazils of this world grow wealthy enough to start enjoying not only the necessities but also some of the luxuries of life. On the other hand, we seem to be entering a period of huge technological advances in emerging fields such as biotechnology that could greatly increase resource productivity and more than offset the effect of growth on the environment. The trouble is, nobody knows for sure.

Since uncertainty will define the coming era, it makes sense to invest in ways that reduce that risk at relatively low cost. Governments must think seriously about the future implications of today's policies. Their best bet is to encourage the three powerful forces for sustainability outlined in this survey: the empowerment of local people to manage local resources and adapt to environmental change; the encouragement of science and technology, especially innovations that reduce the ecological footprint of consumption; and the greening of markets to get prices right.

To advocate these interventions is not to call for a return to the hubris of yesteryear's central planners. These measures would merely give individuals the power to make greener choices if they care to. In

practice, argues Chris Heady of the OECD, this may still not add up to sustainability “because we might still decide to be greedy, and leave less for our children.”

Happily, there are signs of an emerging bottom-up push for greenery. Even such icons of western consumerism as Unilever and Procter & Gamble now sing the virtues of “sustainable consumption.” Unilever has vowed that by 2005 it will be buying fish only from sustainable sources, and P&G is coming up with innovative products such as detergents that require less water, heat and packaging. It would be naive to label such actions as expressions of “corporate social responsibility”: in the long run, firms will embrace greenery only if they see profit in it. And that, in turn, will depend on choices made by individuals.




Such interventions should really be thought of as a kind of insurance that tilts the odds of winning that great race just a little in humanity's favour. Indeed, even some of the world's most conservative insurance firms increasingly see things this way. As losses from weather-related disasters have risen of late (see chart 8), the industry is getting more involved in policy debates on long-term environmental issues such as climate change.

Bruno Porro, chief risk officer at Swiss Re, argues that: “The world is entering a future in which risks are more concentrated and more complex. That is why we are pressing for policies that reduce those risks through preparation, adaptation and mitigation. That will be cheaper than covering tomorrow's losses after disaster strikes.”

Jeffrey Sachs of Columbia University agrees: “When you think about the scale of risk that the world faces, it is clear that we grossly underinvest in knowledge...we have enough income to live very comfortably in the developed world and to prevent dire need in the developing world. So we should have the confidence to invest in longer-term issues like the environment. Let's help insure the sustainability of this wonderful situation.”

He is right. After all, we have only one planet, now and in the future. We need to think harder about how to use it wisely.

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Chief financial officers

# Too creative by 50%?

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AP

**Chief financial officers need to get back to counting beans**

IN EACH recent corporate scandal, a chief financial officer (CFO) has turned up in the hot seat. Scott Sullivan (above, on the right) is under investigation by the Securities and Exchange Commission (SEC). His chummy relationship with Bernie Ebbers, his boss at WorldCom, was dubbed “the Scott 'n' Bernie show” by Wall Street. Andrew Fastow (left), the genius at devising special-purpose entities for Enron, is also under investigation. In better days, *CFO* magazine, a sister publication of *The Economist*, awarded each of them a *CFO* “excellence award”. At Xerox, which overstated its profits by $1.4 billion, Barry Romeril's retirement as CFO in December has not spared him an SEC letter asking why he should not be charged with fraud.

Why are so many CFOs in trouble? “Unlike everyone else in the organisation, they don't have deniability,” says Julia Homer, editor of *CFO*. “The chief executive can always say, ‘I didn't know what was happening.’” That is certainly part of the story. But the role of the CFO also changed in the 1990s—in a way that set the scene for trouble.

A decade ago, most CFOs had a professional accountancy qualification. Today, that is much less common. Last year, Peter McLean, who leads the CFO practice at Spencer Stuart, a firm of headhunters, looked at the qualifications of CFOs at Fortune 500 companies. He found that only 20% were Certified Public Accountants; 35% had MBAs, and 5% had both qualifications. Mr Fastow had a master's degree in business administration from Northwestern University's acclaimed Kellogg School of Management; Mr Sullivan had a degree in business administration from the State University of New York; Dan Cohrs, CFO at Global Crossing, another troubled firm, had a swanky doctorate in finance and public policy from Cornell University.

**A decade ago, most CFOs had a professional accountancy qualification. Today, that is much less common**

This shift is unlikely to be reversed, if only because few people today want to be accountants. Fewer members of the American Institute of Certified Public Accountants, the industry's trade body, are in public practice than in 1989. The institute says sadly that only 1% of high-school students want to major in accountancy, compared with 4% in 1990. It has launched a campaign with the improbable slogan, “Be a Star...Be a CPA” in a bid to attract more.

An accountancy training encourages respect for numbers; an MBA breeds creativity. In the 1990s, the role of the CFO moved away from financial reporting, in ways that made a broad business training more useful. CFOs became strategic planners, playing a big part in mergers; taking charge of information

technology; devising complex financial instruments; and above all, managing relations with investors. “Star quality is the key to raising money,” reflects Steven Hall of Pearl Meyer, a pay consultancy. “It's even more essential now.”

Lynn Turner, a former chief accountant at the SEC, is aghast at the ignorance of basic accounting principles in many companies. He describes how he was telephoned by a company in Texas that was fighting the SEC and its auditors. “The [company's] attorney told me that the CFO had no training in accountancy—he was an operations guy,” recalls Mr Turner. “I said, ‘then they need to call God, not me'.”

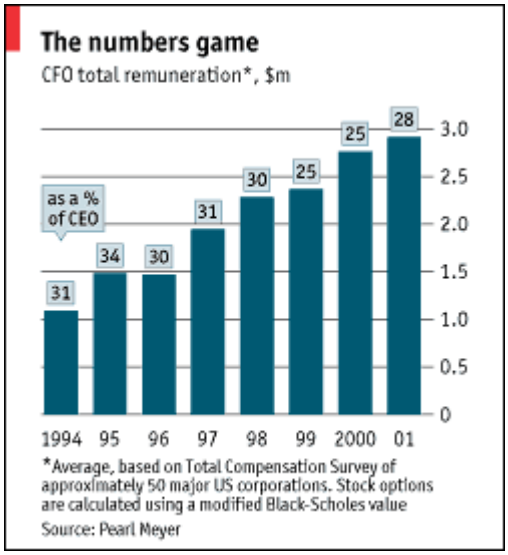
The next best thing may be to appoint a CFO old enough to remember the trade. Several companies have done this. EDS, a services giant, brought in Jim Daley, a grandfather who had been one of the top team at PricewaterhouseCoopers, a large accounting firm, in 1999; Xerox, without a CFO since December, hired 59-year-old Lawrence Zimmerman; in May, Ford brought 67-year-old Allan Gilmour out of retirement.

Another option is to bring in a foreigner. “In Britain, finance directors seem to be more loyal to their practice than to their firm,” observes Frank Schroeder. Now president of DBM Europe, a human-capital consultancy, he worked at Waste Management during that company's financial traumas in the mid-1990s. The newest CFO at an American giant is Andrew Bonfield, recruited from British Gas to Bristol-Myers Squibb.

## Chief fiddling officer

Ignorance of basic accounting can undermine a CFO's ability to cope with a challenge that many have faced in recent years: pressure to “manage” earnings. Investors are brutal to companies that miss their targets; and a fall in the share price is unpleasant for executives with lots of stock options. Unpleasant for CFOs, too: their remuneration, lots of it in options, has moved up briskly in the past decade, in line with that of chief executives.

Even where companies do not do naughty things to their earnings, the relationship between chief executive and CFO has grown closer. Chief executives clearly want a CFO who will be part of the team. If he isn't, he goes. A survey by *CFO* magazine in 1999 found that 39% of chief executives had fired their last CFO, and 75% had hired the current incumbent—40% of them within the previous three years.




Incoming bosses often bring in their own person. That need not be sinister: in May, Bill Ford, chief executive of Ford Motor, replaced Martin Inglis, an ally of Ford's previous boss, Jacques Nasser, with Mr Gilmour. Mr Inglis was the fourth CFO in under three years. iVillage, an Internet company, is on its sixth since 1997; Unisys has had four since 1995.

Against impatient investors and a trigger-happy boss, the best defence of the CFO ought to be the audit committee, the group of (supposedly) independent directors who monitor the company's figures. After a bunch of scandals in the 1990s, American companies revamped their audit committees: they now meet on average 4.6 times a year, instead of 3.5 times in 1998, and only 13% of members have personal or business ties that might compromise their objectivity, compared with 28% in 1998. But still they fail. Enron's audit committee was chaired by Robert Jaedicke, a former accounting professor at Stanford University (where Enron's audit failings have become a popular case study).

To be effective, says Nell Minow of The Corporate Library, a corporate-governance research group, audit committees should hold some meetings without executives. The CFO should report to the committee as well as to the chief executive, and the audit committee should have a say in his hiring and firing. And if CFOs were required to have an accountancy qualification, just as a general counsel must have legal training, they might be more likely to present the numbers honestly.

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Vivendi Universal

# Maître dethroned

Jul 4th 2002 | LONDON AND PARIS
From The Economist print edition

**Jean-Marie Messier's resignation may not be the end of the media group's troubles**

Get article background

A SENSE of self-importance and a talent for self-publicity are not usually handicaps in the media world. But, after Jean-Marie Messier at last quit Vivendi Universal this week, the debt-laden sewage-to-Hollywood group of which he was chairman and chief executive, he conceded not only that he had done "a bit too much, a bit too quickly" but that his media profile had been "excessive". The man who embraced his nickname J6M—Jean-Marie Messier, Moi-Même, Maître du Monde—e-mailed disillusioned staff on July 2nd to confirm that he had, with "infinite sadness", resigned. His successor, Jean-René Fourtou, previously vice-chairman of Aventis, a Franco-German drug company, was confirmed at a board meeting the next day.

The assault on Mr Messier was led by the company's North American shareholders, pushed by the Bronfman family, the value of whose 5.05% stake in Vivendi has shrivelled from *euro*3.37 billion ($3.0 billion) at the beginning of the year to *euro*979m today. But it was the belated decision by the French board members to ditch him that sealed his fate. One key actor, Claude Bébéar of AXA, joined the board this week. Mr Messier's eviction also bore the mark of the French political right, now firmly back in power and fearful for the future ownership of particular bits of the business—telecoms, utilities and Canal Plus, a pay-television operation.

Any idea that Mr Messier's departure and the installation of Mr Fourtou might bring a swift end to Vivendi's troubles is, however, misplaced. It is saddled with a massive *euro*19 billion of debt. After an initial rise in the company's share price, Vivendi's shares sank, at one point losing 40% in a single day (partly in response to a newspaper article claiming that the company had tried to massage its accounts). More important was an announcement by Moody's, a rating agency, that it had downgraded Vivendi's debt to junk status.

In a complete U-turn from its previous more favourable views, Standard & Poor's (S&P) , another rating agency, said on July 2nd that a "lack of clarity" from Vivendi had been rectified and that there had been "unexpected" additions to its near-term financing needs. Management turmoil and weak markets had made a bad situation worse. Vivendi's main businesses are operating profitably, said S&P, but that will be insufficient to sort out the debt crunch. Guy Deslondes, the agency's leading Vivendi analyst, said that the group has no more than two months to find "several billion" euros of new credit lines. The situation has been exacerbated because, it seems, the purchase last December of the entertainment assets of USA Networks from Barry Diller included an off-balance-sheet guarantee of up to $400m due next year to Mr Diller.

The upshot is that, whatever Mr Fourtou might plan to do, Vivendi's fate is now in the hands of its creditors, chief among them Société Générale and BNP. Each is reckoned to have over *euro*1 billion of exposure, and their shares duly fell this week.

A firesale of assets seems unavoidable. The group's best bit may be Vivendi Environnement. Until recently Vivendi owned a controlling 63% stake. But its dash for cash has seen that dwindle to nearer 40% as it has made successive sales. Not only has Vivendi ceded control, it has also hit a political barrier, in the form of government stipulations that any buyer must be French. Any sale of the group's 44% stake in the telecoms group, Cegetel, would also be problematic. The only plausible buyer is Britain's Vodafone; but telecoms are not exactly popular these days.

The media assets that Mr Messier assembled are far from worthless. In Universal Studios, the studio

behind “A Beautiful Mind”, Universal Music, whose roster includes Eminem, Sting and U2, and USA Networks, which makes “Law and Order” and owns the USA and SCI-FI cable channels, Vivendi has three strong content-providers. The music business as a whole is in trouble, partly because of online piracy, but Universal is the market leader and brought in *euro*6.6 billion of revenues in 2001. Box-office receipts in America this year have soared by 20% on last year, with Universal getting at least its fair share.

Already the word is that Mr Diller, the Hollywood veteran who now runs the business, is considering making a bid for the movie assets. More problematic might be the disposal of music for which Mr Diller has no particular appetite. European antitrust regulators seem not to favour further mergers among the five music giants that dominate the industry.

As for the loss-making Canal Plus, it has a strong brand, and is the only pay-TV company with a dominant market position in several European countries, including France and Spain. (Vivendi had already announced a sale of the Italian operation to Rupert Murdoch, though he is now renegotiating the price.) Potential buyers include Lagardère, TF1 and Mr Murdoch's BskyB. Yet Canal Plus's heavy losses, cultural status and statutory obligation to finance French cinema present a big challenge for outsiders. Nothing's easy to sell when you're in distress.

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Weblogging

# The trees fight back

Jul 4th 2002
From The Economist print edition

**Should old media embrace blogging?**

BACK in the mists of early Internet history, online publishing was going to wrest power from the inky fingers of old media groups and put it in the hands of ordinary people. Well, it never happened. Yet just when old media began to feel smug again about its old-fashioned paper-based products, weblogging (known as blogging) happened. The question for the big media world is whether to embrace the phenomenon that, in part, claims to undermine it.

Blogging, the publication of running commentary on personal online weblogs, has in the past couple of years exploded from a cultish techie activity into a cottage industry churning out increasingly compelling content. In 1998, there were about 30,000 weblogs; today, there are some 500,000, according to Cameron Marlow, who runs blogdex, which tracks them.

Blogging has taken off thanks to the development of online tools, such as Blogger and UserLand, which make it simple and cheap to update personal web content instantly. Weblogs range from the political (InstaPundit, Kausfiles, AndrewSullivan) to the high-tech (Dan Gillmor's eJournal, Scripting News, 802.11b, Boing Boing), and from the personal rant to the thoughtful critique. One recurring theme is their quirky, counter-cultural nature. As a recent article in the *Online Journalism Review* put it: “Weblogs are the anti-newspaper.”

Many thrive on correcting or deriding content published in newspapers and magazines. “Blogs have emerged as an instant critique of major media,” says Andrew Sullivan, former editor of the *New Republic*, whose weblog book reviews can lift a title into the top ten on Amazon. “At the same time, bloggers are parasites on big media, relying on them for stories and raw material.”

How then is big media to respond? Some publishers, such as the *San Jose Mercury News* and Britain's *Guardian* newspaper, were quick to set up weblogs. But the general response has been to ignore them. This was not entirely foolish: weblogs do not make money. Some bloggers earn commissions on items bought through a link from their weblog, or receive donations from charitable readers. But even Mr Sullivan says his weblog brings in only about $6,000 a month from such sources. Most bloggers do not blog for money.

So what do big media groups stand to gain from adopting a format that delights in promoting competitors' content, and relies on relinquishing editorial control? Such a question, say bloggers, misunderstands the force of weblogs. “Traditional publishing is about putting on a show; building a network of weblogs is like hosting a party,” says Simon Waldman, head of digital publishing at the *Guardian*.

For all the costly and failed efforts by media companies to create and charge for online material, blogging suggests that the web works best as a link to other people—and a way of finding and raiding their content. As InstaPundit's Glenn Reynolds says, “the threat to big media is not to its pocketbook but to its self-importance.”

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Xerox

# Corruption without contrition

Jul 4th 2002 | STAMFORD, CONNECTICUT
From The Economist print edition

**Why Xerox is still struggling**

AP

**Ms Mulcahy sells well, but when?**

AS AN early pioneer of the accounting fiddles that have been so upsetting markets, Xerox has made good use of its headstart. In the two years since a company insider blew the whistle about how it accelerated revenues, the company has changed its auditor, its chief financial officer and its chief executive (twice). It has settled SEC charges, renegotiated bank loans and restated five years' of accounts. Yet doubts linger. After a brief winter rally, Xerox's market price has again slumped below the book value of its assets. Why is it so persistently unattractive?

The corruption of Xerox, an old-line, insular, east-coast maker of printers and photocopiers, shows how far bubble illness spread in the late 1990s. James Bingham, the whistleblower whom the company sacked in August 2000, alleges that Xerox monkeyed about with its accounts to disguise a deteriorating trading record. The SEC claimed that this was part of a scheme to enrich managers.

Xerox settled these charges in April by paying a $10m fine, but without admitting wrongdoing. The restated accounts, which the company filed on June 28th, show that this “misapplication of GAAP”, as Xerox calls it, overstated profits by $1.4 billion between 1997 and 2001. As these fiddles mostly involved pulling future revenues forward, the restated accounts should help Xerox in the next year or two, as it puts back profits borrowed from the future.

The second big task facing Anne Mulcahy, the Xerox sales veteran who took over as chief executive in July 2001, was to repair the company's finances. So far, so good. The company has struck a deal with GE Capital that will eventually remove from its books most of the equipment financing that has weighed down the balance sheet. Last month, Ms Mulcahy shook hands with her bankers on new loan agreements. The terms are more costly and restrictive, but she will not mind that. There is now enough cash to keep Xerox going for another year or so. Ms Mulcahy says she wants to return to the capital markets, from which the company has been barred, well before then.

That, in part, depends on her third big task: rebuilding the business. Xerox's turnaround plan, she says, is mostly finished. The company has sold assets, laid off tens of thousands of workers and outsourced everything from manufacturing to (wisely, perhaps) internal auditing. These economies have cut more than $1 billion a year from costs. Ms Mulcahy says the company is now in good shape to compete with lean rivals such as Canon and Ricoh.

Ms Mulcahy has bet on two things: first, the market's shift from monochrome to colour printing, where Xerox is concentrating its R&D dollars; second, Xerox's own move from low-margin manufacturing to more lucrative services. For now, she says, about a quarter of the company's sales include some sort of service element. This figure, Xerox hopes, will eventually double, as more big companies outsource the storage, retrieval, printing and management of their documents to Xerox.

But the market remains tough. Although IT spending is no longer falling, it is not rising either. Manufacturers are pushing colour digital printing, says Gilles Biscos of Interquest, a consultancy. In the printing industry, however, customers are struggling to pay for existing equipment. The money they do spend, says Mr Biscos, tends not to favour Xerox. To save costs, printing firms have been lashing

together low-end printers instead of buying high-end models. Xerox is most comfortable in the high-end market, where it does not jostle so much with its Japanese competitors.

Ultimately, it may be the company's seeming inability to make a clean break with its past that weighs most on its share price. It has taken the Xerox bureaucracy (known as Burox) a long time to come out of denial. Barry Romeril, the chief financial officer during the late 1990s, did not leave the board until last December. The company continues to fight a wrongful dismissal suit brought by Mr Bingham. Publicly, Xerox still says it did nothing wrong. It is never wise to say you are sorry in a society as litigious as America's. That is a pity. As the white weatherboard churches of New England preach, before redemption comes contrition.

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Containers

# Ports in a storm

Jul 4th 2002
From The Economist print edition

**America's moves to screen containers abroad are straining logistics**

NEW anti-terrorist security measures in container ports are threatening to play havoc with manufacturers' just-in-time production systems. European exporters fear that the eight days now allowed for shipments to cross the Atlantic could soon stretch to two weeks.

Their fears were first aroused last month, when America's customs service began placing its own officers in Antwerp, Le Havre, Rotterdam and Singapore. The American officers are liaising with local customs authorities to pinpoint containers that might be carriers of death and destruction into the heart of America. The new security measures could add up to a week to the time it takes to clear the ports. This uncertainty disrupts the budgets and planning of companies' shipping managers, who have to juggle transport and inventory costs with transit times.

Cargo manifests that now follow ships when they are at sea will, if new American legislation is passed, have to arrive 24 hours before any America-bound ship is even loaded in a foreign port. Chris Koch, chief executive of the World Shipping Council, which represents the leading container-shipping lines, says that ship owners will have to learn to be firm with exporters, who have in the past “squeezed the system” to get faster and cheaper shipping.

Under its Container Security Initiative (CSI), America is concentrating on the top 20 ports, from which it receives 70% of the 9m-10m containers that arrive on its shores every year. Robert Bonner, the Customs Commissioner, on a whistle-stop tour of Europe last week, sought to play down fears that he is creating a two-tier system, introducing a competitive advantage for the first members of the CSI“club”.

Yet even if the CSI is not an exclusive club, the long list of ports now seeking membership will take some time to process. This gives an enviable advantage to those that are already participating. Mr Bonner tacitly accepts that this will happen, but says that America had to start somewhere. As customs officials execute a U-turn so that they can inspect outbound cargo instead of inbound, the world trading system is facing an unprecedented test of its efficiency.

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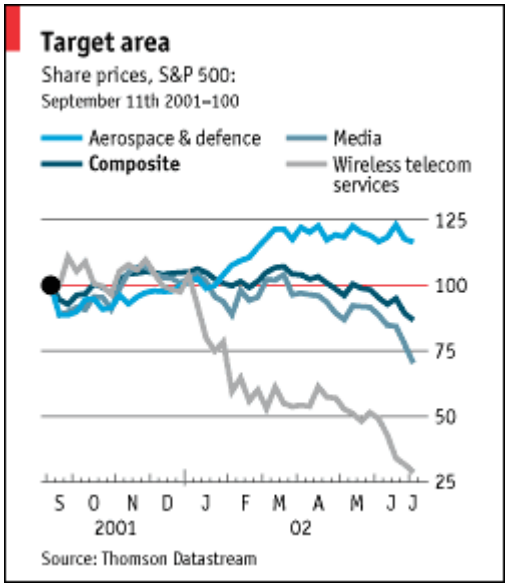
America's defence industry

# On manoeuvres

Jul 4th 2002
From The Economist print edition

**Not everybody is averse to a bit of M&A**




MERGER activity has plunged in America over the past few years, but the defence industry is still enjoying a round of couplings, helped by relatively strong share prices since last September's terrorist attacks. This week's agreed takeover of TRW, an aerospace and car-parts company, by Northrop Grumman accounts for about a quarter of the top ten deals announced so far this year, measured by value. The deal follows four months of dithering after TRW refused a first offer and before Northrop raised its price.

There was a dramatic wave of defence-industry mergers in America in the 1990s, after the Pentagon gave warning that defence procurement would fall steeply (in the event, by more than half) thanks to cuts after the end of the cold war. The Clinton administration eased the pain of these mergers by helping to finance the job cuts that came with them (known as “pay-offs for lay-offs”). The fall-out from all this is behind today's wave of smaller mergers.

The consolidation of the 1990s whittled down what was a group of about 15 companies to five so-called “prime contractors”, the firms that take overall responsibility for each weapons programme, even though much of the hardware comes from subcontractors. These five are Lockheed Martin, Boeing, Raytheon, General Dynamics and Northrop Grumman.

The merger wave came to an end in 1998, when the Clinton administration blocked the purchase of Northrop Grumman by Lockheed Martin because it was worried about a lack of competition. Northrop had sought refuge in the merger after suffering two big reverses. First, it was excluded from the contest to build America's Joint Strike Fighter-at over $200 billion the biggest-ever defence contract (it was eventually won by Lockheed). Then it was told that the air force did not want many more of its B-2 bombers. That left it trailing a weak fifth behind the four leaders.

This week's deal marks the culmination of a strategy to recover from that position through acquisition. Northrop's boss, Kent Kresa, had the foresight to spot that the defence industry not only had to adapt to spending cuts after the end of the cold war, but also to focus on providing hardware and electronic systems for a new kind of warfare, in campaigns such as that in Afghanistan.

After the Lockheed merger was blocked, Northrop went on the offensive, buying two shipyards, Litton Industries and Newport News, in 2000 and 2001. Mr Kresa sees ships as more than “platforms” for missiles or fighter planes; he sees them playing a key role as communications and surveillance centres in today's more electronics-based warfare. The two purchases have turned Northrop Grumman into the biggest naval shipbuilder in the world, ahead of its arch-rival, General Dynamics.

The Pentagon and the Justice Department have smiled on the company's recent purchases. They should welcome this week's merger too, because bolting on TRW's space and satellite businesses makes Northrop a more formidable competitor to Lockheed, Boeing, Raytheon and General Dynamics. This should go some way to calming fears that the 1990s mergers ended up reducing competition and stifling innovation.

Northrop is not the only defence company in America to be making acquisitions. BAE Systems (formerly British Aerospace, but now selling more to the Pentagon than to Britain's defence ministry) and a young company called L-3 Communications have both been growing by snapping up electronics and communications parts of Lockheed Martin. Lockheed Martin got itself into such difficulties integrating the companies from which it was formed that it was forced to sell businesses to cut its debt by some $4 billion.

One business it sold was Loral, whose former boss, Frank Lanza, then set up L-3 Communications by persuading Lockheed's boss, Vance Coffman, to sell him some of the company's other assets. L-3 is now emerging as a sizeable defence group, with sales of $2.3 billion last year. Analysts are projecting 30% annual growth in future. This is to come mostly from the company's systems for improving security at airports and from its continuing purchase of small defence suppliers.

BAE, for its part, is being allowed unique access (for a foreign company) to the American defence market. It was a potential bidder for TRW (as were General Dynamics and Raytheon), in an effort to become a prime contractor. The Pentagon had given its approval; but that was before Northrop produced its winning bid.

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**Weil, Gotshal & Manges**

# Mopping up

Jul 4th 2002 | NEW YORK
From The Economist print edition

**A firm of New York lawyers is at the centre of America's corporate cleansing**

IF THE extended party of the 1990s provided an ideal environment for venture-capital firms and investment banks, the hangover provides opportunities for the kind of firm that can mop up the mess. None is proving more suited to the occasion than Weil, Gotshal & Manges, a firm with 950 lawyers known particularly for its work on bankruptcy and corporate governance. Among its more interesting clients at the moment are Adelphia, Global Crossing, PG&E (a California utility), Kmart's creditors, WorldCom and Enron. Other Wall Street law firms are fishing in the same pool, but none nearly so deeply or successfully.

Fees for this kind of work are not trivial. Global Crossing is paying Weil $2m a month for sorting out a worldwide business that is under investigation by an untold number of regulators, but which may, in the current environment, rank as only a relatively modest disaster. Enron, the most spectacularly complex bankruptcy ever, is paying Weil $6m a month for the work of over 100 lawyers in five countries. They are enmeshed in two gigantic tasks. The first involves unearthing the viable businesses buried in the broad corporate muck; the second, prioritising the mountain of claims from creditors.

The bankruptcy business was radically different in the late 1960s when Ira Millstein persuaded two friends, a New York University law professor called Charles Seligson and a then unknown lawyer named Harvey Miller, to join him at Weil, then a mid-sized corporate-law firm. In the years that followed, Manville, Texaco, Olympia & York and Drexel Burnham Lambert all became clients. Mr Miller became one of the most sought-after lawyers in America and Mr Millstein played a big part in developing standards for corporate governance, particularly the responsibilities of boards. As the lead partner of Weil, he was responsible for the firm's overall growth, an important component of which was the unusual inclusion of a restructuring division.

People wonder what such a strategy produces in good times. Martin Bienenstock, one of the co-heads of Weil's restructuring department, retorts that “the notion that our business goes up and down with the economy is cocktail-party myth.” Instead, he says, there are three main forces that determine the level of large corporate bankruptcy work: liquidity in the high-yield market; a big unexpected change (airline deregulation in the 1970s, deflation in the 1990s); and the volume of underwriting and acquisitions on Wall Street (inevitably producing bad deals that become exposed years later).

As understanding of causes has improved, so too has the ability to resolve consequences. It was not all that long ago, Mr Bienenstock says, that bankruptcies began with an extended period of “debt denial” by creditors, followed by agonising negotiations over how much debt the bankrupt company could ultimately service, followed by “negotiator fatigue” and, finally, after three years or so, a reorganisation. Nowadays, formerly tough creditors such as banks can use new markets to dump loans quickly. The value of the core business is then determined equally quickly, expendable divisions are sold, and a settlement is signed.

Enron, with its arcane accounts and relentless deals, was a poster child for the flaws in the American economy, but it may also be an example of the system's ability to resolve problems as well. Mr Bienenstock says that he had hoped to complete the restructuring within a year, and even though this seems increasingly unlikely, he still believes it might be possible. Given the vast overhang of misbegotten Wall Street deals from the recently concluded boom, he will probably have no trouble finding a client to replace the Houston energy-trading disaster.

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**Face value**

# Called to account

Jul 4th 2002
From The Economist print edition

**Bob Herz faces the daunting task of restoring confidence in American accounts**

"ARE you nuts?" was the response of close friends of Bob Herz when told that he was accepting the job of chairman of America's Financial Accounting Standards Board (FASB). Mr Herz, after all, was leaving a safe position as a senior partner at PricewaterhouseCoopers, the world's largest accounting firm, to step into the heart of the current crisis of confidence in corporate America. Only last week, WorldCom and Xerox announced the two largest profit restatements in history. This week, on July 1st, Mr Herz took up the job of steering American accounting standards in a safer direction. Nuts? Probably not. Brave? Certainly.

Ever since Enron, the bust energy-trading company, admitted last year that its numbers for the previous five years were wrong, FASB has been under attack. It takes too long to push through changes to Generally Accepted Accounting Principles (GAAP), the rules under which American companies draw up their accounts, says even such a conservative as Harvey Pitt, chairman of the Securities and Exchange Commission (SEC). Moreover, others say, its standards are too complex and detailed, allowing companies to evade the spirit of accounting principles, even as they keep just within the strict letter of the rules.

In the past, critics say, FASB has been too vulnerable to the influence of the big accounting firms, which, along with industry, provide a third of its funding. It has already begun to react to such complaints. Under Mr Herz's predecessor, Ed Jenkins, it reverted to requiring only four, rather than five, of its seven board members to agree upon a standard in order for it to be passed. Its "supermajority" vote (introduced, some say, at the behest of the big accounting firms) had crippled its power to set tough standards. The change should uncripple it a bit.

Mr Herz intends to push further. For a start, he wants to overhaul the framework within which standards are set. At the moment, no fewer than four different organisations issue standards. He says that the number needs to come down, and that FASB's primacy should be reasserted. One reason why he was picked for the job is that he believes that principles, not rules, should feature more heavily in American standard-setting. That view won the support of the SEC's chief accountant, Bob Herdman, for his appointment. These days the SEC is, not surprisingly, taking a close interest in FASB and its standard-setting procedures.

Described by fellow accountants as an anglophile, in spite of his New Jersey origins, Mr Herz learnt his accounting at Manchester University in Britain. British accountants hold that the principle that a company's accounts should provide a "true and fair" view of its underlying economic position should take precedence over detailed rules.

Mr Herz will not, however, find it easy to steer the GAAP juggernaut in the direction of similarly broad principles. Trevor Harris, a valuation and accounting analyst at Morgan Stanley in New York, argues that the entire book on lease accounting could be replaced by one simple sentence—"all non-cancellable obligations must be capitalised"—if Mr Herz only had the support to do it. But trying to dump big chunks of existing GAAP rules in this way would cause an outcry, not least because companies and auditors like

to have such rules as a protection against lawsuits. The best that he can hope for, perhaps, is that the emphasis will shift in future standards.

## Bridging the GAAP

To the surprise of his then colleagues, Mr Herz recently turned down the chance to run for the position of chairman of the global board of PricewaterhouseCoopers. To do this he would have had to resign from his part-time membership of the International Accounting Standards Board (IASB), an organisation whose cause—creating a single set of high-quality standards for the whole world—he is passionate about.

He admits that international standards are not yet good enough for America to accept them. But he will continue to promote them at FASB. He says that he wants to move quickly to identify the main differences between GAAP and international rules, so that he can then focus on what he calls the “low-hanging fruit”.

In some areas, Mr Herz's desire for convergence with international standards will be controversial. Sir David Tweedie, chairman of IASB and a personal friend, believes that stock options should be charged as costs. So does Mr Herz, though he adds that valuing them is a puzzle. Later this year, IASB will issue a draft proposal to that effect. Mr Herz is then expected to seek to follow IASB's lead on this and other sensitive areas—such as the simplifying of accounting for financial instruments, including derivatives.

He knows that his drive for reform will set him against the many groups that take a strong, sometimes unhealthy, interest in the setting of accounting standards: big business, for example, politicians and the accountants themselves. He harks back to FASB's darkest hour, in 1994, when a heavily lobbied Congress forced the board to issue a standard on stock options that it knew to be wrong, because it did not treat them as an expense.

From a technical, accounting point of view Mr Herz is thought brilliant, especially in the field of financial instruments. But his ability to manage in a charged political environment is unproven. Some of his supporters fret that his jovial, easy-going manner may lack the gravitas required to cope with corporate and other lobbying. Amid the current swirl of accounting scandals, Mr Herz could hardly have a better platform for promoting reform. Still, if he is to rescue American accounting, comments Lynn Turner, a former chief accountant at the SEC who is now an academic, the new head of FASB will need “the fight of a tiger and the slyness of a mongoose.”

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East Asian economies

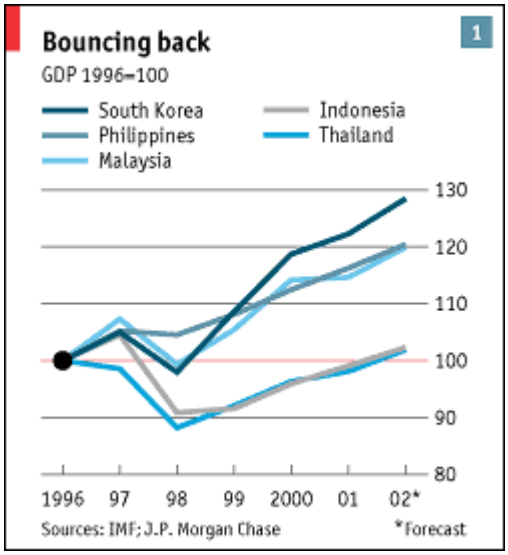
# The lost (half) decade

Jul 4th 2002 | BANGKOK AND TOKYO
From The Economist print edition

**Five years after East Asia's financial crisis, much of the region seems to be doing fine. But it still needs banking and other reforms**

WHATEVER happened to the East Asian crisis? After Thailand devalued the baht on July 2nd 1997, capital rushed out of the region's economies, and in rapid succession most of them collapsed. The resulting panic soon spread beyond East Asia to other emerging markets, and for a while it posed a serious threat to the world economy. And yet five years on, the most striking thing is how well many countries are doing, despite a stuttering global economy. South Korea's GDP last year was nearly one-quarter bigger than in 1996. For many, the 1997-98 crisis now seems little more than a blip (see chart 1).

Admittedly, for two decades up to 1997, the region had enjoyed eye-popping success, mainly by following Japan's path to export-led growth. As each new economy joined the so-called “flying geese”, the flock seemed to fly faster. But the events of 1997-98 shattered the illusion that the geese were unstoppable. So how have they managed to get back into the air?




One answer is that the International Monetary Fund, which failed miserably to foresee the crisis, deserves some credit. Its emphasis on tight fiscal and monetary policies was controversial, but its advocacy of a swift disposal of bad debts was spot on. The main hold-out against IMF policies was Malaysia, and in practice it followed the Fund's advice without taking its money. And although Malaysia's capital controls grabbed the headlines, they were imposed after the currency had fallen sharply and foreign capital had fled, making them relatively unimportant.

## Good news from the east

The most obvious good news is that the macroeconomic situation of the crisis countries has improved dramatically. Besides the resumption of GDP growth, external finances are much sounder. The pile of short-term foreign-currency debt that triggered the 1997-98 panic has largely been repaid or rescheduled. Most currencies are no longer fixed. And many central banks have bolstered their foreign-currency reserves.

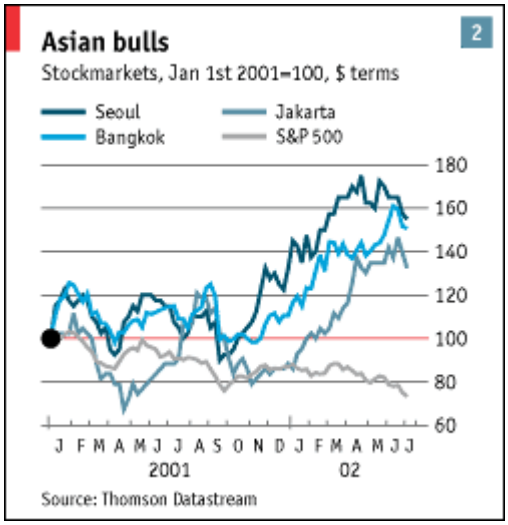
Politically, too, East Asia has stabilised a bit. In the aftermath of the crisis, long-standing governments fell in South Korea, Taiwan and, most dramatically, Indonesia. Thailand acquired both a new government and a new constitution. Previously unthinkable protests broke out in Malaysia. The turmoil continued last year, when Indonesia and the Philippines jettisoned their presidents in mid-term. Yet politics in the region has settled down, for now.

Although most of the region's currencies are no longer linked to the dollar—Hong Kong, which is, along with Malaysia, the main exception, has fought off several attacks on its peg—the combination of better short-term finances and political stability has made exchange rates less volatile. Interest rates and inflation are low. This is not to say that Asia has shed its financial worries. In several places, serious banking problems have yet to be dealt with, and growth in business lending is still moribund. Moreover, in Thailand, Indonesia and the Philippines, varying degrees of doubt have emerged about the longer-term soundness of public finances.

Yet at least East Asia no longer seems quite so dependent on outside forces to keep it flying. The end of America's runaway expansion, marked by a drop in technology investment, has not hammered the region as hard as many feared. That is partly because Asia's crisis-stricken economies are rebuilding trade with each other. Although Japan remains comatose, rapid growth in China's relatively small trade is adding to demand. These trends have helped exports to rebound from their drop in 2001. So far this year they have risen by more than 20% in local-currency terms in South Korea, Malaysia and the Philippines, according to David Fernandez, a regional economist at J.P. Morgan in Singapore.

Mr Fernandez reckons that growth in exports will soon slow, as demand for business investment remains weak. His bank forecasts only 6% growth in global capital-equipment spending over the next 18 months, two-thirds the growth rate of the late 1990s. Yet many East Asian economies, notably South Korea, have been offsetting America's downturn in another way, by booking impressive growth in domestic consumption. This combination of local and intra-Asian demand has bolstered confidence amid the global slowdown, and portfolio capital continues to flow in. Even as bourses in Europe and America have slid, some Asian stockmarkets have charged ahead (see chart 2).

After 1997-98, such hot money is not always welcome, however. And there are other clouds in the sky. It is not certain that Asia's declining inflation rate (according to Andy Xie, an economist at Morgan Stanley in Hong Kong, it has fallen to 2.2% over the past five years, from 8.6% in 1990-96) is an unambiguously good sign: some countries are grappling with deflationary pressures. Mr Xie also points out that, even as exports by China's neighbours have risen sharply in local-currency terms, their dollar value has remained stagnant. To achieve the same dollar GDP as before, those countries have had to offset depreciating currencies with higher export volumes. Their current accounts have swung into surplus, allowing them to pay down foreign debts, largely because imports—an important source of capital equipment and other investment—have slumped (see chart 3).




Even so, East Asia's export orientation and high investment proved more successful, over several decades, than the protection or profligacy that some other emerging-market governments, for instance in Latin America or India, espoused. Nor should the East Asians fret over China's recent success at attracting the dragon's share of foreign investment. It could yet abate, as it has in many other regions (including emerging Asia) that seemed perennial magnets.

Still, without questioning their commitment to free trade, many East Asian business and political leaders are wondering how much they need to modify the rest of their economic model. To understand their choices, it is worth taking a close look at the only goose that has set off in a clear direction since the crisis: South Korea.

## The Korean example

For all their national loathing of the IMF, Koreans' response to the crisis was to embrace the IMF's financial reforms and make them their own, from the newly elected government to banking and business leaders, and even to the unions, which eventually acquiesced in many of the changes. The contrast with Japan's inertia of the 1990s was not accidental. The Korean government stepped in to recapitalise the banks, and to set up a public asset-management company to buy up bad loans. Of the 156 trillion won ($129 billion) that it has injected into the system, the government expects to retrieve around 56%, largely by reselling equity in banks and recouping a portion of their bad loans and collateral. It is retiring its bail-out-related debts ahead of schedule. More importantly, however, this has freed the banks to get on with business.

They have done so by using their fresh capital and healthier loan portfolios to begin lending again. Just as crucially, Korean banks overhauled their practices, making it more likely that their new loans would be put to better use. In particular, they have made two changes for the better. The first is in the way they allocate credit. Before, the government directed them to lend money to cherished conglomerates. Close political links and an unhealthy bias towards export industries eventually led to huge misallocations.

After overhauling the banks' balance sheets, the government not only stopped doing this, but also took several steps to foster deeper changes. Financial regulators laid down guidelines for managing credit risks, including independent credit committees insulated from the boss's meddling. The banks too embraced them. The government has also forced conglomerates to purge the debt from their balance sheets, by selling entire divisions, narrowing their focus, and in some cases going out of business altogether. That has broadened the banks' corporate lending, making it easier for small and mid-sized firms to borrow.

The second big change the banks have made is to respond more keenly to competitive pressures. Although a few big bank deals never materialised, private-equity investors and foreign banks have nevertheless taken stakes in a number of Korean banks, and even the independents have consolidated operations, cut costs and bolstered their marketing. With this has come a new emphasis on consumer lending, which now accounts for around half of Korean banks' loan book. This trend has brought worries about indebted consumers, especially users of credit cards. But the benefits to the domestic economy have outweighed these risks.

South Korea's East Asian neighbours have noticed its recent success. Yet there is a danger that they will draw the wrong conclusions, emulating the changes least relevant to their condition. South Korea's booming domestic economy has clearly helped cushion it from the global downturn, and given its consumers and workforce fresh confidence. But it was an all-out effort to reform the financial system that triggered the change, not the other way round. Meanwhile, without having fully cleaned up their own bad-debt mess, several of South Korea's neighbours are hoping to bypass the pain and give their own domestic economies a direct boost.

This would be a mistake, for two reasons. First, it will be hard for South-East Asian economies to restore credit growth and investment without resolving their bad-debt problems. Contrast South Korea's performance, for example, with that of Indonesia. That country's banks were hit harder than any others; yet it has been the slowest to deal with the problem. As a result, large piles of industrial assets are still stacked up in its misnamed “Bank Restructuring Agency”. With many bad debts still unresolved, and little sense of who will end up owning what, it is hard for sound businesses to get fresh capital.

The region's other economies lie somewhere in between. In Thailand, as in Indonesia, nobody is sure what claims a creditor really holds until the courts are through. A series of bankruptcy reforms was just beginning to take hold when the new government set up its own asset-management body last year, to try to centralise collection of the remaining bad debts. After originally embracing the idea, many private bankers have backed away. Malaysia has made an effort to clean up corporate debts, along the lines of Korea's approach. Indeed, the government's forceful efforts to push through some deals differed sharply from the Indonesian and Thai approaches. But by continuing to mix business with politics, Malaysia's government has frittered away much of the boost in confidence it might have earned.

South Korea's neighbours have not only been slow to address past bad loans. By failing to resolve the banks' problems, they have also delayed their adjustment to the future of Asian finance. That future will probably involve a continued shift away from bank borrowing by big companies. Having been burned once, the healthy ones have been raising capital in the equity and, even more eagerly, bond markets. Those large companies that still want to borrow from banks tend to be the ones that no sensible banker would lend to. If they are to prosper in the future, therefore, East Asia's banks must become far better at serving small and medium-sized borrowers along with consumers, as Korean banks are already doing.

The need for these changes, however, extends far beyond the banks themselves. The way East Asia's economies have collected and channelled savings needs an overhaul. One of the most telling statistics, argues Keith Irving, an analyst at Merrill Lynch in Hong Kong, is the high ratio of bank deposits to bank lending. That the region is sitting on so much liquidity reflects not only the lingering effects of the banking crisis on loan growth, but also the continuing refusal of Asians to move their money out of bank deposits. If East Asia is to upgrade its economic model, savers must begin to channel more of that money into bonds and equities.

As their economies prosper, South-East Asia's venerable savers might also start to feel a little freer about spending their cash. Yet because they are so much less developed than South Korea, those economies cannot realistically hope to enjoy the sort of booming domestic-led growth that their new favourite goose is enjoying. And it is here that South-East Asian leaders are beginning to make their second big mistake, using government spending to yank their economies in the direction of domestically driven growth.

Throughout East Asia, governments are desperately keen to get domestic demand going again. Early in the crisis, demand fell sharply, and a general push for fiscal austerity may have contributed to that. When Thailand's and Malaysia's governments began to spend more freely, this may have helped to reverse their slide.

## The perils of public spending

Now, however, several South-East Asian governments may be painting themselves into a fiscal corner. The Thai government has toyed with several new spending schemes, including a potentially unsustainable health-care entitlement. Perversely, it is even considering import duties to plug its fiscal deficit, while stalling on much-needed privatisation. After regaining investor confidence with tight budget targets last year, the Philippines' government has recently lost control of the reins. And Indonesia's government continues to rely on aid money for life support.

These countries risk more than just higher public-debt burdens—though once again they should beware of following in Japan's footsteps. By relying on the public sector, they also risk turning their backs too quickly on the best source of future prosperity: trade. Unlike South Korea, the financial-market distortions in many South-East Asian economies led to excessive investment in domestic sectors even more than in export ones. Poorly regulated Thai finance companies, and banks run by Indonesian business tycoons, channelled money into office buildings, golf courses and other speculative local projects, inflating the property bubbles that helped to ruin their economies.

For South-East Asia, therefore, trade, especially intra-regional trade, still offers the best way forward. In this context China's rapid growth should be a blessing, not a threat. “For a lot of these countries...” says Mr Fernandez, “openness and outward-orientation is still the surest way to increase per capita incomes, and domestic demand will take care of itself.”

Of course, maintaining the right kind of “outward” orientation is now harder than it was when the rest of the emerging world hid behind trade barriers. China's growth, especially, will create huge shifts in comparative advantage, to which its neighbours must adapt. They can make great strides, however, merely by straightening out the corruption and warped incentives that push capital into the wrong places. If export earnings are scarce, Indonesia's poor treatment of foreign mining and energy companies is all the more inexcusable. If the Philippines has an advantage in telephone call-centres, eliminating red tape and corruption will help attract the foreign investment it needs.

Only in Malaysia, with a slightly more advanced economy and smaller debt bubble when the crisis hit, could a case be made for emulating South Korea. Indeed, giving incentives for housing loans early in the crisis may have been one of the government's best policies, and—along with a surge in car loans and retail spending—helped to restore domestic demand. Yet even in Malaysia, the pump-priming has lately got out of hand.

The best reason to hope for progress is that East Asian countries have laid the groundwork over the past five years for increased accountability. New governments have come in across the region, with only a couple of exceptions, and the shock of the regional collapse has made Asians more wary of sweet promises.

Besides improving political accountability, the crisis has also raised awareness among domestic investors, who will be keen to improve transparency and corporate governance in the companies they are asked to invest in. Though foreign complaints help, more clamouring by domestic investors has the best chance of pushing further capital market reforms.

The recent outbreak of stability also helps. It would be far better if things moved faster, but for the moment at least the region seems at reasonably low risk of big reversals. With the turmoil of the immediate post-crisis years behind them, therefore, East Asia's economies have a chance to build on the foundation they laid in the boom years—if they keep liberalising and clean up the lingering financial messes that still hold them back.

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Accounting scandals and the SEC

# Harvey Pitt fights back

Jul 4th 2002 | NEW YORK
From The Economist print edition

Getty

**Lambasted for doing too little, the chairman of the Securities and Exchange Commission may yet overreact**

Get article background

THE accounting scandal at WorldCom has caused misery for investors, creditors and employees of the telecoms firm. Harvey Pitt appears to see it as a great opportunity. In his first ten months as chairman of the Securities and Exchange Commission (SEC), America's chief markets regulator, Mr Pitt has been attacked for failing to show leadership in tackling the glaring failings of Wall Street and of America's corporate bosses. Critics accused him of dragging his feet because, they alleged, conflicts of interest led the securities lawyer to put his former private clients—especially the big audit firms—before the public interest. WorldCom has given him a chance to show that he is in charge and on the right side.

“There's a very tough cop on the beat here,” thundered Mr Pitt on any television show that would have him, after WorldCom admitted on June 25th that it had falsely boosted profits by $3.8 billion. Promising to “clean this mess up”, he announced that the company would be prosecuted for fraud, and that the SEC would go after the millions of dollars that executives earned as a result of their own fraud. “The American public is outraged,” he says. “And in my view, criminal charges may be too good for the people who brought about this mess.” His conversion has prompted much scepticism, not least among Wall Street folk surprised to hear such black-and-white statements from a man so nuanced in the shades of grey that make up America's securities laws.

Perhaps Mr Pitt's new assertiveness is down to politics. The constant criticisms of his performance may not have penetrated what he admits to be a thick skin. But they were certainly starting to harm George Bush's administration and Republicans at large, with mid-term elections for Congress due in November. Did his White House masters tell him to make a better show of representing the public interest?

Maybe. Or maybe Mr Pitt is now far more worried about a loss of public confidence in the capital markets than he was even a month ago. His recent activism may be part of an urgent effort to avoid a further erosion in confidence—and with it, presumably, more falls in shares. After all, further scandals are surely coming.

Perhaps, strange as it might seem, Mr Pitt has not really changed at all. Perhaps the criticism made of him before the WorldCom mess was wrong. Far from being a lackey of Wall Street and of the accounting industry—placed at the SEC by a pro-business administration in order to unwind much of the activism in

favour of small investors pursued by his predecessor, Arthur Levitt—might it be that Mr Pitt's current activism is what he planned all along?

The way Mr Pitt tells it, events have just accelerated his agenda (in part, he says, because there is now a greater consensus about what is needed) and shifted some of his priorities. Yet even before the discovery of fraud at WorldCom, he was claiming to preside over the most activist commission since its establishment in 1934. His pursuit of a radical agenda, he says, was largely ignored by the media. Since he early on promised a gentler, less confrontational SEC, perhaps that is not surprising.

Asked now about how America's securities laws should be reformed, he jokes that they could be replaced with a simple, two-part law. Section one: it shall be unlawful. Section two, the SEC shall have the power to define “it”. That will not happen, but it may not need to. For Mr Pitt believes that existing powers, rather neglected by his predecessors, allow him to transform regulation without the need for new laws.

An example of this is his announcement, following the WorldCom scandal, that chief executives and chief financial officers will both have to certify the accuracy of their firm's accounts. This will make it easier for the SEC to launch a criminal prosecution for fraud should accounting inaccuracies come to light. The change will greatly increase the potential punishment facing errant bosses.

Mr Pitt is also driving the reform of accounting standards, something his predecessors largely left to the Financial Accounting Standards Board (FASB), financed by the accounting industry, which has just acquired a new head (see article). The SEC is introducing new requirements for firms to explain the impact of their choice of accounting treatments, and to make them disclose sooner any material changes to their business outlook. Firms will no longer be allowed to hide behind their use of the standard Generally Accepted Accounting Principles if they still manage to paint a misleading picture.

Those who know Mr Pitt find the criticism that he is conflicted by past client relationships amusing. Few people are more committed to their own opinion than is the SEC chairman. He claims that his private-sector past is a strength because “I know where the bodies are”. He may have thought little of having controversial meetings with bosses of firms under investigation by the SEC, such as KPMG, because the notion that his interests might be conflicted did not occur to him.

Mr Pitt's power (and his budget) is likely now to grow. A higher profile will, however, test his political skills in Washington, which have not been all that noticeable. After all, had Mr Pitt's activism to date been more effective, forceful legislation currently being steered through Congress by Senator Paul Sarbanes would have been less necessary—and less likely to pass. The Sarbanes bill is much tougher on auditing firms than are Mr Pitt's proposals—starting with a sterner oversight board and also restricting the consulting work that auditors may do.

And yet. Beyond auditing, some people on Wall Street fret that Mr Pitt may be stung by all the criticism to do too much—in terms of poking a regulatory nose into the activities of businesses—rather than too little. A gentle irony that would be.

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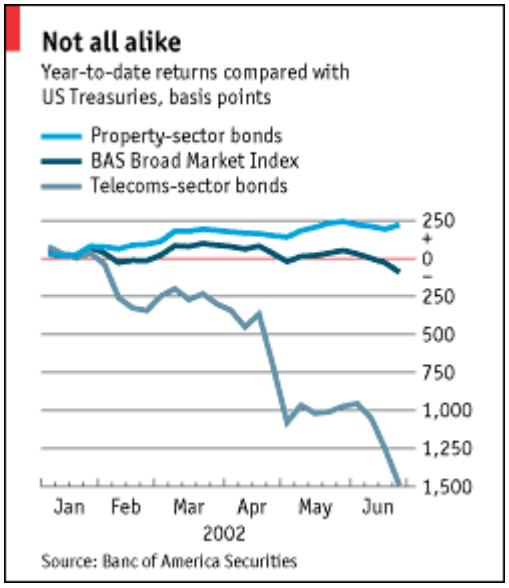
Credit markets

# On to the pyre

Jul 4th 2002 | NEW YORK
From The Economist print edition

**Swift punishment for erring companies, but reward for the just**




THE credit markets continue to punish companies that no longer appear to have robust financial statements. This week Vivendi and France Telecom were added to the pyre, following Enron, Global Crossing and WorldCom. June was already an awful month for parts of the corporate-bond market. Prices of high-yield (ie, junk) debt, for instance, fell by 8%, with the debt of telecoms companies down by one-third. More surprises will come when, from August 15th, senior executives will be held criminally liable for their company's financial statements, and when 2,400 companies, former clients of Andersen, take on keen new auditors.

Although America's economy is still growing, the credit quality of companies deteriorates. Moody's, a credit-rating agency, is currently downgrading the bonds of five companies for every company it upgrades, the worst ratio since 1990.

In the markets, the bonds of some companies have made a precipitous slide towards junk status even as they maintain an investment-grade rating. AOL Time Warner, an Internet, cable and magazine conglomerate, generates torrents of cash to cover its huge debts. Yet after a $54 billion write-off, its bonds, which normally yield around two percentage points more than American Treasuries, now trade over five percentage points more. The bonds, in other words, are behaving like junk, and their potential buyers, say traders, are high-yield investors. Such investors are already swamped trying to analyse a slew of companies that have recently fallen into their domain, including Tyco, Qwest, The Gap and Goodyear.

If there is light in the gloom, it is that, unlike several earlier credit panics, many companies have seen prices for their bonds rise, not fall. Railroads, oil producers, property trusts and even consumer-finance companies have all seen their bonds go up. And America's market for short-term commercial paper—which, thanks to downgrades to the limited number of eligible issuers, had been slowly shrinking in size since the end of 2000—has not been affected by the recent turmoil. In short, the credit markets may be skittish and in many areas deeply morbid. But in sorting through problems and rewarding virtue, they are doing what markets should.

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American banks

# A murky sort of pond life

Jul 4th 2002
From The Economist print edition

**Corporate governance at American banks leaves a lot to be desired**

BANKS in America who lent to companies caught up in accounting scandals should be in a good position to appreciate the value of strong corporate governance. Unfortunately, according to a report by Mike Mayo, an analyst at Prudential Financial, their own record is patchy.

Four out of five chief executives at the 30-odd banks that Mr Mayo examined are also their chairmen. One out of four board members has a financial relationship with his bank. At some, such as FleetBoston Financial and SunTrust, only about half of the directors can be considered independent, according to Mr Mayo.

Worryingly, given the conflicts of interest that bedevilled Andersen, which audited Enron and WorldCom, 70% of the fees that banks pay to their external auditors, on average, are for services other than audit, such as consulting and tax. Most banks have fired Andersen in recent months, but the unhealthy result is that the top nine banks in America are audited by just two firms, PricewaterhouseCoopers and KPMG.

Big banks have two supervisors, the Federal Reserve and the Office of the Comptroller of the Currency. That, chief financial officers say, should allay fears. Investors are not so sure, because banks are so hard to understand. Jim Chanos, a hedge-fund manager who was the first person publicly to cast doubt on Enron's financial statements, says that although he used to sell bank stocks short, he has stopped, partly because banks have increased their trading to such a degree that “you can't see into large banks anymore”—just like hedge funds.

On the lending side, the fact that banks make loans to companies too small to gain access to the capital markets makes their balance sheets harder to fathom. Securitisation, or the practice of bundling and selling more straightforward sorts of assets, such as mortgage receivables, has in one sense made banks more inscrutable, since banks are left with assets that are relatively opaque. The use of derivatives to lay off and buy credit risk can also obscure sources of credit exposure.

Don Morgan, an economist at the Federal Reserve Bank of New York, points out in a forthcoming paper* that the two biggest credit-rating agencies, Moody's and Standard & Poor's, have been more divided over their ratings of banks and insurers than over companies in any other industry. Because banks are opaque, he says, their corporate governance is all the more important.

*“Rating banks: risk and uncertainty in an opaque industry”. *American Economic Journal*, September 2002.

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**Japanese banks**

# Nationalised once, nationalised again?

Jul 4th 2002 | TOKYO
From The Economist print edition

**Interest in buying some Japanese banks, if only the government allows it**

Get article background

WHO wants to buy a Japanese bank? They are barely profitable, and they are weighed down by ¥150 trillion ($1.25 trillion) of bad debts. On July 2nd a credit-rating agency, Moody's, downgraded its assessment of the biggest banks' financial strength to an "E": the lowest you can get. Yet several, mostly foreign, groups are out shopping.

They reckon that the banks' distressed-debt portfolios are full of profitable opportunities. They may also think they can turn banks around by improving their management and corporate governance. A handful of private-equity groups from America have bought bankrupt regional banks. The best-known foreign purchase was made by Ripplewood Holdings in 2000, which caused a stir. It bought the venerable Long-Term Credit Bank, now called Shinsei Bank, one of two big banks that were nationalised in 1998.

Fresh controversy surrounds the other bust bank, Nippon Credit Bank. It too was sold in 2000, to a consortium of investors, led by Softbank, an Internet investment group, Tokio Marine & Fire, Japan's largest non-life insurer, and Orix, a leasing company. Cerberus, an American investment fund, has a smaller stake. Now called Aozora, the bank boasts a former American vice-president, Dan Quayle, on its board. Like Shinsei, Aozora was stripped of many dud assets before it was sold, but was still left with plenty. Both banks were given the option, lasting three years, to hand bad loans back to the government if they lose more than 20% of their value.

A month ago the president of Softbank, Masayoshi Son, told a parliamentary committee that he was thinking of selling his company's 49% stake in Aozora. Softbank, once mighty, has fallen on hard times; its share price has fallen by 97% since early 2000. Aozora now needs a forceful owner. It has not reduced its bad debts as aggressively as has Shinsei, says another rating agency, Standard & Poor's, and it lacks a clear business strategy.

The government wants Tokio Marine or Orix to buy Softbank's stake. Neither is likely to do so. The leading bidder is Cerberus, which already owns 11.5% of the bank. Ripplewood is also thought to be interested. So far, no serious domestic candidates have surfaced.

Cerberus's bid seemed to hit a snag when the *Nihon Keizai* newspaper reported that the Financial Services Agency (FSA) might block attempts by foreign investment funds, out to make a quick buck, to hold big stakes in banks. Untrue, says the FSA, which denies any bias against foreigners. All the same, revised banking laws have something to do with Softbank's toying with a sale. The laws require new investors to get regulatory approval—and current stakeholders to get fresh approval by April 2004—before taking more than a 20% stake in any bank. On top of scrutinising shareholders and related parties, the agency can now inspect sources of funds.

A bigger worry for foreign bidders is a condition that big shareholders "fully understand a bank's social responsibilities": a reminder that Japanese banks have duties other than to maximise profits. The FSA's banking division insists that the rule will not penalise groups such as Cerberus. But critics wonder whether other regulators, regretting that Shinsei and Aozora have "put" options that enable them to use

taxpayers' money to clean up their books, will apply the rule as fairly.

These options were granted by a government that blocked bidders from inspecting banks' books, for fear of exposing the poor health of other banks with loans to the same borrowers. Now the options are causing a headache. Shinsei has been cleaning up aggressively, returning some ¥700 billion of bad loans to the government. Yet as fresh loans sour, its ratio of bad loans to total loans, at 20%, has scarcely fallen. If Shinsei is to meet its bad-debt target of only 5% by next March, when its option expires, it will have to return many more loans.

If too many bad loans are dumped on the state, politicians fear a popular backlash. They also worry about how this might affect the health of other banks. When in 2000 Shinsei returned to the government its portion of loans made to Sogo, it sparked that department store's collapse. Since then, some banks have chosen to buy Shinsei's loans, and so increase their own exposure to stricken companies, rather than risk further bankruptcies among their borrowers.

Aozora has so far not exercised its option as aggressively: Tokio Marine and Orix are wary of a bad press. Yet any foreign shareholder is likely to be much less passive—especially since Aozora's option expires in September 2003. The government may yet be able to persuade Softbank to hold on to its stake, or it might even buy the stake itself: in effect, renationalising the bank. Such a move would leave Aozora with a balance sheet still heavy with debts when its option expires.

Such uncertainty hurts Aozora's funding and may even threaten its survival. Shinsei also has been hurt by recent disputes with the government over some of the bad loans it is trying to return. The spread between their bank debentures (which provide about half their funding) and government bonds has widened in recent months, as investors have demanded bigger risk premiums (see chart on previous page). Aozora is already finding it difficult to extend its funding beyond September 2003, says Jason Rogers of Barclays Capital. None of this, however, seems to have persuaded the government to sort out its muddled policies on insolvent banks, even though more are expected to go down in the coming months.

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**Borsa Italiana**

# Carina

Jul 4th 2002 | MILAN
From The Economist print edition

**Italy's bourse is focusing on domestic growth. This may change**

MERGERS and consolidation often seem to be all that the welter of European stock exchanges and clearing and settlement agencies are thinking about. The London Stock Exchange (LSE) has held talks with Nasdaq, an American exchange. Deutsche Börse is, for the second time, thinking about a merger with the LSE. Euronext now controls four stock exchanges (Paris, Brussels, Amsterdam and Lisbon), as well as five derivatives exchanges, and may be looking for more. This week a big settlement agency, Euroclear, which had been jilted by a rival, Clearstream (now owned by Deutsche Börse), announced a merger with London's Crest, to form Europe's biggest settlement agency. And the London Clearing House (see article) is mulling a merger with Clearnet, its Paris-based counterpart.

There is one exception: Borsa Italiana, Milan's stock exchange and the most coveted of the continental bourses to remain out of the dance. It is Europe's fifth-biggest by trading volume, and sixth-biggest by market capitalisation. Since its privatisation in 1997 it has taken over MIF, Italy's market for interest-rate derivatives (it already owned the exchange for equity derivatives), and has launched a market for high-growth companies. As one of Europe's most profitable stock exchanges, Borsa Italiana contemplates its future—and its continued independence—with a degree of confidence. Is that justified?

The Borsa's head, Massimo Capuano, argues that mergers make little sense when takeover rules, corporate law and accounting practices are so fragmented around the European Union. For instance, even though Euronext now controls several exchanges, each has to be run separately. Furthermore, hopes of a great rise in the cross-border trading of shares have always run too far ahead of reality. Cross-border trading of European shares is something over 15% of the total.

This fragmentation is supposedly being fixed. After a report last year by Alexandre Lamfalussy, a former head of the European Monetary Institute, the European Union is trying to accelerate the process of tearing down barriers to a single capital market. The investment-services directive, a particularly unsatisfactory piece of legislation, is being rewritten. Other priorities of the Lamfalussy report are new directives on prospectuses accompanying the sale of new securities and on market abuses, such as insider trading. Mr Capuano banks on all this taking time and falling well short of perfection.

Meanwhile, the Borsa intends to grow at home. It plans to take over Montetitoli, the settlement agency of which it now owns 4.1%. The Borsa also wants to move from its present core shareholders to a full public listing on its own market, which Deutsche Börse, Euronext and the LSE all have, since that would allow it to raise fresh capital.

Taking over Montetitoli should not be too much trouble. The Borsa's board has already approved the bid. Most of its shareholders also hold a stake in Montetitoli, while the two outfits also have the same chairman. Going public will be trickier. Italy's securities-market regulator, Consob, still opposes a public offering. It has concerns about supervision when the Borsa is traded on its own exchange.

With his plan to take over Montetitoli, Mr Capuano wants to get clearing and settlement under the exchange's roof. In other words, he is leaning towards the German model of a vertical silo—in which a stock exchange oversees not just the trading of securities, but their clearing and settlement as well. Exchanges with a horizontal model, such as the LSE, are independent of clearing and settlement agencies.

Opponents of the vertical silo argue that such a monopoly encourages anti-competitive behaviour; it also may tempt exchanges to cross-subsidise their trading from clearing and settlement profits. They would much rather see mergers of clearing and settlement businesses in different jurisdictions, which could

bring down costs. But defenders of the model answer that a silo, with its straight-through processing, brings greater efficiencies.

Vertical and independent, then, for the Italians. Yet things might change quickly if any of Europe's big three exchanges were taken over by a rival, or if Euronext really were to benefit from a rise in the pan-European trading of shares. In either case, smaller exchanges could not afford to go it alone. And when the Borsa Italiana eventually gets a public listing, shareholders might force the exchange's hand, as Mr Capuano concedes.

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Italian bonds

# Relations unsettled

Jul 4th 2002
From The Economist print edition

**A bitter fight to trade, clear and settle government bonds**

HOW much longer can Italy play dog-in-the-manger with its government-bond market? It is the biggest in Europe, with *euro*1.1 trillion ($1.1 trillion) of bonds outstanding, compared with Germany's *euro*615 billion. Banks in the euro area find that Italy's bonds are the most convenient to offer as collateral when raising cash from the European Central Bank.

So the biggest banks, seeking ever more efficient use of capital, want Italian bonds to be cleared using the same central clearing counterparty (CCP) as for other European government bonds. The ability to offset Italian bond positions against positions in other bonds, futures and repurchase agreements would sharply reduce credit risk with counterparties.

For two years the London Clearing House (LCH), the biggest CCP in Europe, has knocked at Italy's door. But the Bank of Italy insists that its country's bonds be cleared domestically, through the Cassa di Compensazione e Garanzia, which it owns, for settlement with Italy's securities depository, Montetitoli. How very un-European. Isn't this supposed to be a single market?

Yes, but. Based in London, LCH sits outside the euro zone. The European Central Bank, interested Italian parties say, is against euro-area government bonds being cleared outside the zone: the Bank of Italy is falling in line with ECB policy. Not so, retorts the London Clearing House. The central bank's concerns are about domestic CCPs outside the euro zone, not a pan-European counterparty like LCH.

Behind this spat lies rivalry between two electronic bond-trading platforms. BrokerTec in London offers clearing through LCH; MTS, with Italian sponsors, wants to use Clearnet, a Paris-based clearing house. MTS has the lion's share of electronic trading of Italian bonds, while BrokerTec is building a growing share in other euro government bonds. A new product of BrokerTec's, called RepoClear, has encouraged banks to net more bonds and bond-repurchase agreements via the LCH. MTS is understandably worried that bringing Italian bonds into the BrokerTec/LCH ambit could quickly draw all liquidity in Italian bonds on to the BrokerTec platform. There is a precedent: four years ago Liffe, London's derivatives exchange, then floor-based, lost all its volume in the German government-bond futures almost overnight to a cheaper (and electronic) Frankfurt exchange, Eurex.

MTS hopes to set up Clearnet as a central counterparty for Italian bonds by the end of the year, and so to steal a march on BrokerTec and LCH. Gianluca Garbi, chief executive of MTS, dismisses accusations of foul play, but he has accusations of his own. He does not like the corporate governance of LCH, he says, because it is dominated by the big dealing banks; besides, entry costs are high. As for BrokerTec, he says, it is under investigation by America's Department of Justice, along with other dealer-owned trading platforms, for anti-competitive practices. The irony is that the spat would become irrelevant should LCH and Clearnet merge, which seems likely. Mr Garbi professes delight at the prospect, because the governance issues will have to be cleared up, he says.

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**Insurance broking**

# Jackpot

Jul 4th 2002 | NEW YORK
From The Economist print edition

**Willis shows that there's still money being made on Wall Street**

IT SOUNDS implausible. But here is a mainstream American company—a financial one, to boot—whose share price has been hitting new highs. Willis, the world's third-largest insurance broker, has gone from strength to strength since a leveraged buyout four years ago.

That was when Kohlberg Kravis Roberts (KKR) quietly took Willis Corroon, a sleepy insurance broker listed in London, private for $1.7 billion. By the time Willis emerged in June 2001 as a Bermuda-based company with a listing on the New York Stock Exchange, its value had doubled. It has since doubled again. KKR put in about $300m of its own cash, for a 72% stake. In two share offerings, one last November and another in May, the firm raised $870m. It still retains a 40% stake, worth $1.8 billion. That translates into a 77% compound annual return on its investment.

Insurance brokers make money by earning a small percentage of every dollar their clients spend on policies. Keith Trauner, an analyst at Fairholme Capital Management, says that the business can be thought of as a royalty on the total value of companies (companies take out insurance based on the value of their operations), multiplied by prevailing insurance rates. It is not a complicated equation, and over much of the 1990s results were poor, because even as the value of companies grew, insurance rates shrivelled.

Only after the failures in 2000 of Reliance, a large underwriter in America, and several syndicates at Lloyd's of London did the soft pricing cycle turn. Rates hardened further, thanks to American litigation over asbestos and securities fraud. The attacks of September 11th had an immediately brutal effect on underwriting capacity, which shrank in several areas of the market—aviation, marine, energy and reinsurance—even as companies sought more insurance, not less. Willis is a beneficiary of more business and higher rates. Its revenues rose by 17% in the first quarter.

If Willis is not the only insurance broker to have benefited, it has done so more than most. The two brokers that have long dominated the business, Aon and Marsh & McLennan, both had offices in the World Trade Centre and were badly hit by the disaster, losing many staff. Before that, the two firms had spent much of the 1990s buying up second-tier firms. Now their combined market share is nearly 60%—gains they must hold even as they try to integrate their operations. In comparison, Willis is tiny. Although it has grabbed one-third more market share since KKR's acquisition, it still has only 8% of the market.

What is more, neither Aon nor Marsh & McLellan are pure insurance brokers, at a time when diversification hurts. In the past, Marsh earned big profits from its mutual-fund subsidiary, Putnam. Today, Putnam's customers are defecting and its assets are shrinking; its shares have fallen by one-fifth since April. Aon is trying to spin off an underwriting subsidiary, and its shares are down by one-third.

Willis appears still to be reaping the benefits that can come from a leveraged buyout. In October 2000, Joe Plumeri, who had headed retail banking at Citigroup, was brought in. He began tearing out costs, cancelling club memberships and tightening travel rules. More staff were hired—the salesforce is now 2,300, one-tenth higher than last year. Before the buyout, staff had almost no equity in the company. Today they have been encouraged to become owners: three-fifths of the staff have 8% of the company

among them. “I tell everyone, we're not here to make you happy,” says Mr Plumeri. “If you want to build wealth, own shares.”

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Economics focus

# The Fund bites back

Jul 4th 2002
From The Economist print edition

**A notable development: the IMF's new chief economist says what he thinks of Joseph Stiglitz**

Get article background

FOR the past several years, Joseph Stiglitz—renowned economic theorist, Nobel laureate, former chief economist at the World Bank—has been waging a campaign of vilification against the IMF. Bizarrely, this campaign began while Mr Stiglitz was in post at the Bank, the Fund's sister organisation, as the two institutions laboured to devise co-ordinated strategies for dealing with crises in emerging-market economies. Having left the Bank (at the suggestion of America's Treasury), Mr Stiglitz upped the tempo. Interviews and articles poured forth. His most recent thrust is a new book, "Globalisation and Its Discontents", which describes his feelings about the Fund in unforgiving detail.

*The Economist* reviewed Mr Stiglitz's book in our issue of June 8th. This column will not review it again—though it is necessary, by way of declaring an interest, to give a flavour. We said that the book was not about globalisation, as it claimed to be; that its criticisms of the Fund were poorly argued; that it was muddled and badly written; that its tone was unbearably self-righteous; that the policies it proposed were in important instances unworkable; and that it made reckless accusations of personal misconduct that were completely unwarranted. Aside from that, we quite liked it.

Then, on June 28th, an unusual thing happened. Kenneth Rogoff, the Fund's new chief economist and a distinguished academic in his own right, spoke to a group of people at the World Bank who had come to hear him discuss the book with Mr Stiglitz—and he told them exactly what he thought of it. Up to now the Fund has been at pains to maintain civilised relations with Mr Stiglitz. It has expressed its disagreement with moderation and courtesy. Big mistake. Nobody paid attention. Mr Rogoff decided to eschew politeness and try candour. Thus, his comments, since posted on the Fund's website, have attained the status of an instant classic.

They take the form of an open letter to Mr Stiglitz. A sample:

> Let's look at Stiglitzian prescriptions for helping a distressed emerging-market debtor, the ideas you put forth as superior to existing practice. Governments typically come to the for financial assistance when they are having trouble finding buyers for their debt and when the value of their money is falling. The Stiglitzian prescription is to raise the profile of fiscal deficits, that is, to issue more debt and to print more money. You seem to believe that if a distressed government issues more currency, its citizens will suddenly think it more valuable. You seem to believe that when investors are no longer willing to hold a government's debt, all that needs to be done is to increase the supply and it will sell like hot cakes. We at the — no, make that we on the planet Earth—have considerable experience suggesting otherwise. We earthlings have found that when a country in fiscal distress tries to escape by printing more money, inflation rises, often uncontrollably. Uncontrolled inflation strangles growth, hurting the entire populace, but especially the indigent. The laws of economics may be different in your part of the gamma quadrant, but around here we find that when an almost bankrupt government fails to credibly constrain the time profile of its fiscal deficits, things generally get worse instead of better.

Such language will doubtless be called unbecoming. A censorious report in the *Financial Times* made Mr Rogoff out to be the troublemaker: Mr Stiglitz was "dumbfounded" at this personal attack, it said, and dismayed by the Fund's refusal to "engage in a substantive discussion". This seems odd. Mr Stiglitz routinely accuses those who disagree with him of bad faith, professional incompetence, or outright

corruption. And how could he fail to notice the Fund's countless efforts at “substantive discussion”?

This column applauds Mr Rogoff's forthrightness. His remarks may be angry, but they do not lack substance. The paragraph just quoted makes a telling point. So does every other paragraph. For instance, Mr Rogoff charges that Mr Stiglitz, by casting himself as a whistleblower (guaranteeing copious sympathetic coverage in the press), undermined the ability of the Fund and Bank alike to deal with the problems they were asked to confront. This view has support within the Bank as well as at the Fund. And Mr Rogoff is right to reject Mr Stiglitz's oft-repeated accusation that the Fund is a slave to “market fundamentalism”. The IMF's very existence affirms the idea that markets sometimes get things wrong, and that action by public agencies is necessary as a result. The “market fundamentalist” slur is merely a tactic to win applause from undergraduates.

The IMF sometimes makes mistakes, to be sure. It is in the nature of things: the Fund practises battlefield medicine. Mr Rogoff has been among its critics in the past—but, like most others, he has given the Fund credit for doing its best in difficult circumstances. And he always found that it “bent over backwards” to take his arguments on board.

Mr Rogoff is new to the Fund. Soon he may learn to hide what he means between the lines. We hope not. Just in case, enjoy the straight talk while it lasts. The letter ends:

> On page 208, you slander former number two, Stan Fischer, implying that Citibank may have dangled a job offer in front of him in return for his co-operation in debt renegotiations. Joe, Stan Fischer is well known to be a person of unimpeachable integrity. Of all the false inferences and innuendoes in this book, this is the most outrageous. I'd suggest you should pull this book off the shelves until this slander iscorrected.
>
> Joe, as an academic, you are a towering genius. Like your fellow Nobel prize winner, John Nash, you have a “beautiful mind”. As a policymaker, however, you were just a bit less impressive.
>
> Other than that, I thought it was a pretty good book.

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Carbon sequestration

# Fired up with ideas

Jul 4th 2002
From The Economist print edition

**Capturing and storing carbon dioxide could slow down climate change and also allow fossil fuels to be a bridge to a clean hydrogen-based future**

Get article background

IF THE world is to tackle the problem of climate change in earnest, "clean coal" has to become more than just an amusing oxymoron. All fossil fuels contain carbon, but coal is by far the most carbon-intensive. This is troubling, since global warming seems to be driven by an increase in the level of atmospheric greenhouse gases, of which carbon dioxide ($CO_2$) is the most worrisome. Coal is also the most abundant fossil fuel (see chart). If all known conventional oil and gas reserves (those in underground formations, obtained by drilling) were burned, the level of $CO_2$ in the atmosphere would still be less than twice what it was before the beginning of the industrial revolution. Climate change associated with that level of $CO_2$ might be tolerable. Burn all the coal, however, and it would be more than four times that starting-point—with larger, less predictable and quite likely more unpleasant climatic consequences.

Much of that coal will, nevertheless, be burned. In particular, poor countries such as China, India and South Africa have large reserves that are almost certain to be used to fuel economic growth. So it makes sense to consider possible technical fixes to the problem. These will never be the whole answer; unless the correct incentives are applied, burning coal without such fixes is likely to remain cheaper than burning it with them. But combined with the right incentives, in the form of such things as carbon taxes, they could help to keep the rise in atmospheric $CO_2$ to manageable proportions. They may also, surprisingly, help to usher in the green nirvana of a "hydrogen economy", in which the fuel of choice is that non-poisonous, non-greenhouse gas.

**Carbon in, carbon out**

Energy resources*

| | Resource base, GtC† |
|---|---|
| Oil (conventional) | 241 |
| Oil (unconventional, eg tar sands) | 407 |
| Natural gas (conventional) | 253 |
| Natural gas (unconventional, eg coal-bed methane) | 509 |
| Coal | 5,151 |

Potential $CO_2$ storage reservoirs

| Sequestration option | Worldwide capacity‡ GtC† |
|---|---|
| Ocean | 1,000s |
| Deep saline formations | 100s-1,000s |
| Depleted oil and gas reservoirs | 100s |
| Coal seams | 10s-100s |

*Proven reserves plus likely future resources
†1 GtC=1 billion tonnes of carbon equivalent
‡Orders of magnitude estimates

Sources: UNDP World Energy Assessment, 2000; Howard Herzog, Massachusetts Institute of Technology

## Catch me if you can

Technological solutions to rising atmospheric $CO_2$ (as opposed to, say, planting forests to soak the stuff up through photosynthesis) come in two parts. The first is capture: extracting the gas from the machine that is burning it. The second is sequestration: putting it somewhere it cannot easily escape from.

Capture is the more expensive of the two, especially when it needs to be designed into a plant from the start. One method that can be retrofitted on to existing machinery (although it is probably worth doing so only for large emitters) is to "scrub" $CO_2$ from an exhaust by passing it through a chemical, such as mono-ethanolamine, which has a particular affinity for the gas.

Smaller $CO_2$ sources (such as car engines and homes), which account for about half the gas generated by burning fossil fuels, are unlikely to be susceptible to retrofitted scrubbing. And even in large plants, scrubbing is easier and cheaper when the exhaust has a high concentration of $CO_2$—which is not the case for fuels that have been burned in air. Some have suggested using pure oxygen rather than air, but that is hardly an economically practical solution.

In some ways, though, a truly practical solution is even more radical: to change the way that energy is extracted from fossil fuels by separating the $CO_2$ formation from the process of heat generation. That can be done by adapting a well-established chemical process known as steam reformation. This involves reacting a carbon-based fuel with oxygen and steam to produce a so-called "synthesis gas" that is composed of carbon monoxide and hydrogen (much of the latter comes from the water, rather than the fuel). That mixture can be separated quite easily, and the hydrogen burned in, for example, a gas turbine. Then, mixing the carbon monoxide with more steam in the presence of a suitable catalyst yields $CO_2$ and still more hydrogen; again a mixture that can be separated quite easily.

It is this idea, known as the integrated gasifier combined cycle (IGCC) approach, that has environmentalists excited. It would require big changes to the design of energy-generating equipment, and so could not be introduced quickly. But it is not pie in the sky. And true visionaries will notice that, since it produces hydrogen, it permits the generation of electricity by fuel cells (chemical reactors that create electrical current from the reaction between hydrogen and oxygen, without any harmful emissions) as well as conventional gas turbines. Fuel cells are a critical component of most projections of what a hydrogen economy might look like.

Although the whole package seems idealistic, most of the technologies involved are in fact already in common use, in such processes as ammonia production. Indeed, there are several IGCC plants already operating in Europe and America (although they do not bother to remove $CO_2$). Some firms are talking of building one in China. Robert Williams, head of energy-systems analysis at Princeton University, reckons that, even in countries such as China, where tackling global warming is not exactly a priority, such gasification could lead to "zero emissions from coal", helped on its way by the extra revenues that may come from so-called "polygeneration" of clean synthetic fuels, hydrogen and electricity together.

## Down under

Scrubbing and gasification can thus deliver $CO_2$ in a form that can be disposed of. Actually doing so, though, remains a challenge. Leaks from $CO_2$ repositories would hardly be as disastrous as leaks from a nuclear-waste dump. Nevertheless, to be effective, those repositories would have to stay gas-tight for centuries.

One way of disposing of the gas might be to **sink it beneath the waves**. The oceans already store a lot of $CO_2$, so they might be induced to accept a little more. But it would have to be buried in water that is not likely to come to the surface any time soon. Some scientists worry, though, that dissolving vast quantities of $CO_2$ in the bottom of the ocean could result in ecological damage; others fear that the gas will be regurgitated wherever it is put. An international research consortium planned to test such worries by releasing 60 tonnes of $CO_2$ on the seabed near Hawaii—but noisy protests forced it to cancel the plan last month. Howard Herzog of the Massachusetts Institute of Technology, a member of the consortium, says that the team now hopes to shift to the North Sea.

A less speculative option would be to use **depleted oil and gas reservoirs**. These are layers of porous rocks topped by a cap of impermeable rock, usually in the shape of a dome. After decades of oil exploitation, there are plenty of ageing fields around. The advantages are many: the geology and technology involved are well understood; the exploration costs are small; and the reservoirs in question have already proved they can hold liquids and gases for aeons, since that is how the extracted hydrocarbons built up in them. What is more, injecting $CO_2$ into such wells could produce a saleable by-

product; a similar technique is already used by oilmen to squeeze extra output from declining sources. For example, EnCana, a Canadian oil company, pays the Dakota Gasification Company to pump $CO_2$ produced at Dakota's coal gasification plant by pipeline to some of its wells.

In what may prove to be a straw in the wind, an American emissions brokerage called CO2e.com announced this week the largest-ever public trade in the emerging greenhouse-gas market. Ontario Power Generation, a Canadian company, bought the right to the emissions-reduction "credits" associated with 9m tonnes of $CO_2$. That gas, produced as a by-product of natural-gas processing, would normally have been vented into the atmosphere, but it will now be injected instead into old oil-fields in Wyoming, Texas and Mississippi. The power company has volunteered to cut its emissions of greenhouse gases, and sees these credits as a way to offset its fossil-fuel emissions.

A similar idea to burying $CO_2$ in old oil wells is to inject it into **coal seams** that are too deep and uneconomic to mine. This has two attractions. First, the injected gas will be absorbed on to the surface of the coal, and so locked up more or less permanently. Second, the incoming $CO_2$ often displaces methane that would otherwise not have seen the light of day. Capturing and selling that methane could turn this approach into a nice little earner. A scheme in New Mexico already uses $CO_2$ in this manner.

Also promising are **saline aquifers** located deep below the earth's surface. $CO_2$ pumped into such places would dissolve, at least in part, in the salt water. In some such formations, it would also react with local silicate minerals to form carbonates and bicarbonates that could stay put for millions of years. Statoil, a Norwegian oil firm, has been pumping $CO_2$ into a deep saline aquifer under the North Sea since 1996—the first time "geological" sequestration of this sort has been motivated by a fear of climate change, in the form of a Norwegian tax on carbon emissions. That tax created the incentive for Statoil to bury the stuff rather than continue releasing it into the atmosphere.

Geological sequestration, then, is not merely a speculative idea. In some cases it may even pay part or all of its own way, by releasing otherwise inaccessible fuel deposits. Recognising this, eight big energy companies, led by BP, have recently formed the $CO_2$ Capture Project to promote research. The Natural Resources Defence Council, a big American green group, says it is keeping an open mind about this sort of sequestration. And there is one other important endorsement: "We all believe technology offers great promise to significantly reduce emissions—especially carbon capture, storage and sequestration technologies." Thus spake George Bush, the man who said No to the Kyoto treaty on climate change.

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**Embryology**

# Left, right or wrong

Jul 4th 2002
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**A source of bodily asymmetry has now been revealed**

THE human body may be beautifully symmetrical on the outside; internally, however, it is anything but. The heart is to the left, the liver to the centre-right, the troublesome appendix lurks low down on the right—at least in 99.99% of people. The remaining few have a condition called *situs inversus*, in which right and left are confused and the organs are laid out in a mirror-image of the normal arrangement.

Research published in this week's *Nature* describes how this pattern is imposed at an early stage of embryonic development. Shigenori Nonaka and his colleagues at Osaka University in Japan studied mouse embryos. They found that the direction of fluid flow across an embryo is what differentiates left from right. They could induce *situs inversus* in growing mice simply by reversing the direction of this flow.

The left-right axis of an embryo is established at the time when it is beginning to develop its central nervous system (seven days after fertilisation, in the case of mice). The key to the process seems to be a structure known as the node. This is a depression at one end of the developing body that is coated in rows of hairlike structures called cilia. These move in time with one another, each rotating at 600 rpm. This co-ordinated motion causes the surrounding liquid to flow to the left. Since one result of this movement is to waft chemicals from one side of the embryo to the other, and since such chemicals include those controlling the details of development, it is an obvious possible cause of asymmetry.

To test this idea, Dr Nonaka and his colleagues used a type of mouse whose cilia are paralysed by a genetic mutation. These mice display *situs inversus* half the time, which is suggestive. But to prove that the rotation of the cilia controls lateralisation, the researchers did an experiment.

They placed embryos of mutant mice in an artificial flow of fluid that mimicked the effect generated by cilia. The tiny proto-mice were held steady against this current by placing them in small traps. They were allowed to develop in the flow for about 12 hours, and then cultured normally. Then they were examined when they were almost ten days old—by which time some of their organs were sufficiently developed to see what was going on. The embryos' sense of direction had been restored by the artificial fluid flow: their organs were developing on the correct sides of the left-right axis.

To confirm this result, the researchers put some embryos into the traps back-to-front. The flow of fluid was in the opposite direction to natural cilia-driven motion. Lo and behold, these mice grew into *situs inversus* specimens. And, having shown what could be done with mice whose cilia are paralysed, they moved on to look at healthy mice. They found they could swap left and right in these embryos, too, although they had to use stronger currents to overwhelm the efforts of the cilia.

Inverted mice generally live happy and healthy lives, so long as all their organs are swapped over. However, when the transformation is incomplete (a condition called *situs ambiguus*) the misplacing of body parts causes complications. In people with this problem, heart defects are common. And even those who are perfectly mirrored often suffer respiratory problems that are, independently, associated with defective cilia. So, although the research was carried out on mice not men, the same mechanisms are probably at work in all vertebrates.

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**Hand-washing**

# How to save 1m children a year

Jul 4th 2002
From The Economist print edition

### Just add soap and water

THE second-biggest killer of children in the world is neither malaria, nor tuberculosis, nor AIDS. It is the runs. Diarrhoea kills the equivalent of a jumbo-jet full of children every four hours. Development specialists have known this for years, and struggled to prevent it by diverse means: easier access to water for washing, better health education, oral rehydration therapy and so on. Now, it seems that the best solution may also be the simplest: persuading people to wash their hands with soap.

Obvious, really. But not in developing countries, where most households have soap of some sort but only 15-20% routinely use it to wash their hands after going to the toilet, cleaning a dirty baby or undertaking other tasks that spread potentially lethal bugs. Even in rich countries, people do not wash their hands with soap as often as they should: fewer than half of British mothers will do so after changing a nappy, and only one person in three remembers after a trip to the loo.

Yet a literature review carried out by Valerie Curtis and her colleagues at the London School of Hygiene and Tropical Medicine (and not yet published) finds that appropriate hand-washing can cut diarrhoeal diseases by 43%. It may have an equally big impact on respiratory-tract infections, the biggest child-killer of all. A huge study carried out for the American army found that sniffles and coughs fell by 45% when troops washed their hands five times a day.

But how to persuade people to scrub? Two years ago, at a World Bank forum on hygiene and health, Dr Curtis suggested a global partnership between soap makers and sanitation experts. Development officials had always tended to emphasise the role of the public sector in improving public health. But it is the private sector that builds most of the world's toilets and sells its soap. A previous public-private partnership, involving three big soap companies, had worked well in Central America. Dr Curtis began with a trial in two places: Ghana, in West Africa, and Kerala, a relatively developed state in southern India.

Bringing together all those concerned with encouraging hand-washing turned out to be a revelation. The private-sector soap companies and the government officials and health workers found it hard to understand each other at first. The ponderous bureaucracy of officialdom dismayed the soap companies. The bureaucrats misjudged the difficulty of getting rival companies to work together.

Now the World Bank is backing a programme in Ghana to promote hand-washing. The Indian and Keralan governments are raising $8m-10m for a similar three-year programme in Kerala. The soap companies think sales could grow by 40% in each market.

The health experts are bowled over by the marketing prowess that the companies are bringing to the project. Together they have, for instance, understood that Ghanaians prefer liquid to solid soap for hand-washing and are more likely to wash their hands before eating if the soap does not smell too strong (since Ghanaians often eat with their hands). They have also calculated that an ideal time to change a mother's habits is when a new baby arrives (because she is then more receptive to new ideas and also in more frequent contact with health workers). They have learnt when and how often to show advertisements to have maximum impact. And they have realised that families may want to buy soap in very small quantities—perhaps like a sweet wrapped in paper—because some dislike sharing toilet soap and others cannot afford to buy big bars.

Once the programme has been rolled out in the first two places, it will be extended to China, Nepal, Peru, parts of Central Asia and Senegal. According to Dr Curtis, soap is a sort of do-it-yourself vaccine. And profitable and affordable, too.

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Treating a stroke

# It takes more than prayers

Jul 4th 2002
From The Economist print edition

**Strokes can cause paralysis, speech loss and depression. But the intensive therapy patients need often isn't there, as Sheila Hale discovered when her husband fell ill**

SIR JOHN HALE was a distinguished historian, charming, civilised and eloquent. At 69, just a month after he completed his masterwork, “The Civilisation of Europe in the Renaissance”, a massive stroke left him scarcely able to utter more than two syllables of nonsense, although his understanding of language, both spoken and written, remained unimpaired.

Before that, Sir John had been a natural star, who was widely admired as a teacher and lecturer. His American wife, Sheila, younger by 15 years, had no hesitation in deferring to him: “For more than half my life, I had taken John's superior intellect and imagination for granted. John was my encyclopedia, problem solver, the window through which I enjoyed life.” Extraordinarily, he remained a star. Although never able to say much beyond his two syllables, he conjured the illusion of intelligibility. With gestures, facial expressions and all the rhythms of normal speech, he would “converse”, occasionally bursting into hilarious set pieces, miming, imitating, doing accents, even singing the parts-convinced (until he heard tapes of himself) that the meaning he so clearly intended was clothed in words.

The Man Who Lost His Language
By Sheila Hale

*Allen Lane; 302 pages; £14.99*

Buy it at
Amazon.co.uk

“The Man Who Lost His Language” is a moving and frightening book, with implications that go well beyond the personal trauma that gave rise to it. In Britain, more than 140,000 people this year will have a stroke for the first time; in America, the figure is 750,000. Some are paralysed; most will face speech problems, depression, severe pain. Treatment is slow, and carers, who may feel frightened and helpless themselves, often come under great emotional, financial and physical pressure. Lady Hale calls her book “a kind of love-letter”, and so it is, though it is a difficult and lonely kind of love. Their friends were charmed by him, but she couldn't let it go at that. Having known him as John, the crack in his mind obliged her to know him as a brain-”that unlovely organ that apparently makes us all what we are”. She owed it to him to discover the science behind his disability and, if possible, to fix it.

And so a large part of this book is about “aphasia”, meaning “without language”, about the history of its

diagnosis and treatment, about the theories of where and how the brain organises language, and about language itself in all its modes-heard, spoken, written, read. Reading these impressively researched chapters, it is impossible not to be dazzled by normality-by the head on your shoulders. Lady Hale writes, for example, of an aphasic woman who could talk about what she heard and write about what she read, but could not write about what she heard or talk about what she read; a man who could not name an object in his left hand if he could not also see it. The bizarre particularity of language-loss suggests that our expressive souls are mapped on to grey matter with absolute precision. Why can someone say a word when it is used as a noun, but not when it is a verb? Or name the musical notes in the key of G, but not the same notes in the key of F?

But this is not Oliver Sacks country. Lady Hale's point is not the wonder of it, but the treatment of it. She says, at the end, that if she were to write the book again, she would make it angrier-though it is angry enough as it is. Institutional defeatism ruled from the start. “Put him in a home,” one consultant advised. As she points out, an ageing, stroke-prone population-16% over 65, rising to 20% by 2020-is being served by a medical profession that is far more comfortable dealing with those illnesses that can be easily treated by drugs, technology or surgery. Speech therapy is left largely in the hands of “pleasant young women”.

As Joan Brady described in “Death Comes for Peter Pan”, a lightly fictionalised account of how her husband was cared for while he lay dying, America is no better. But Lady Hale's sharpest criticism is for Britain's National Health Service-in her opinion, hierarchical, paternalist, accountant-driven, and, what is more, allowed by an undemanding population to get away with it. She met some remarkable and dedicated professionals, but it took heroic determination to save John Hale from the neglect of the system. Her verdict is withering: “I do not believe that any society that treats its old and helpless citizens the way they are treated in Britain deserves to call itself civilised.”

The Man Who Lost His Language.
By Sheila Hale.
*Allen Lane; 302 pages; £14.99*

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**Mars**

# A rose-red, dried-up world

Jul 4th 2002
From The Economist print edition

**Get article background**

A CENTURY ago, Mars seemed a fascinating place—home to an ancient civilisation advanced enough to build huge irrigation canals and warlike enough, perhaps, to invade the earth. But those days are over. Telescopes and spacecraft have revealed that Mars is a dead, dry, cold planet, of interest only to collectors of pinkish-brown rocks. How, then, did Oliver Morton manage to write such a lively and accurate book about the red planet? Easy—by focusing on people.

The heroes of Mr Morton's book are the astronomers who yearn to solve Mars's scientific puzzles, the science-fiction writers who project their politics on to Mars's blank canvas, and the space-flight enthusiasts who dream of Martian colonies. It is a book about people for whom Mars matters.

Among them are the computer wizards who interpret the digital streams of data from satellites. These have shown that Mars had vast oceans in the past, and went on to demonstrate, after this book went to press, that Mars still has lots of ice beneath its surface. Mr Morton, a former science editor of *The Economist*, introduces the scientists who argue about how the oceans vanished, and whether Mars once had living creatures. The book is written with enthusiasm and in a graceful style. The best chapters are those that report from the scene, such as the day the flight team for the Mars Polar Lander realised that their beloved spacecraft had crashed and a convention of the Mars Society, which Mr Morton regards as "an undeniably utopian and escapist organisation, and there is nothing wrong with that."

The few sections about rocks are harder to follow. This is partly because the illustrations are poor. Whole-Mars images, extolled as "maps to lose yourself in, like windows in a spaceship's floor", are reproduced only two inches high. This is especially unfortunate as maps are central to the book—the links between the dry, dead rocks of Mars, and the living beings on earth who are smart enough to study them, even while trapped (temporarily, perhaps) in their own faraway world.

JOSH WINN

Mapping Mars: Science, Imagination and the Birth of a World.
By Oliver Morton.
*Fourth Estate; 351 pages; £18.99.*
*To be published in the United States by Picador USA in September*

Mapping Mars: Science, Imagination and the Birth of a World
By Oliver Morton

*Fourth Estate; 351 pages; £18.99.*

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**Lucian Freud**

# Bare flesh, hidden soul

Jul 4th 2002
From The Economist print edition

**Lucian Freud exposes his subjects, but reveals virtually nothing of himself**

THE paintings in the Lucian Freud retrospective at Tate Britain have been acclaimed by critics as the work of a genius. They believe without reservation that Mr Freud is the nation's greatest living painter. And in many ways he is.

Mr Freud revived depiction of the nude and has single-handedly kept alive the grand tradition of figurative painting while rumours of its death abounded. His gestural paintwork has been compared to Rembrandt's, though Mr Freud's subjects—mainly close family and friends—display none of the Dutch master's warmth. When painting his children, he says in the catalogue, he sought to avoid “Titusitis”, the name he gives the sentimentality that he believes marred Rembrandt's paintings of his son.

Today Mr Freud's painterly gravitas seems an increasingly valuable commodity in an age, indeed in a gallery, where conceptual installations and video art attract ever more attention. His canvases possess the reassuring patina of traditional art: the painter's touch, his Old Master references. Yet Mr Freud's work remains resolutely modern, depicting the human form as simple flesh, stripped of pretence and protection, beautiful in its ugliness, reality laid bare. As Frank Auerbach, a friend and fellow painter, writes: “The subject is raw, not cooked to be more digestible as art”.

To wander through room after room of raw, human flesh in the gloaming half-light of a London afternoon feels almost sepulchral, for the painter has insisted that there be only natural light. There is no gentle gloss, no sliver of human sympathy, in these paintings. Each is the product of obsessive concentration. As Mr Freud said to the show's curator, William Feaver, “I want to go on until there is nothing left to see.” Confronted with the physical immediacy of the models, we are forced to see them at odd angles through the painter's devouring gaze. Many of his children, as well as his various wives, lovers, friends, pets and the odd posh client, such as Baron Heini Thyssen, are meant to be seen and not heard. Mr Freud does not believe in descriptive titles or explanations. Looking at his painting is the only point. If you want a story, read a book.

Yet for an exhibition which even Mr Freud calls “autobiographical”, the artist at the heart of it remains especially difficult to penetrate. He shuns interviews, speaking mainly to Mr Feaver, who is writing his biography. Unlike Picasso, who acknowledged his many children and mistresses by name, Mr Freud likes to gloss over many of his relationships. It is unclear how many children he has fathered, or by how many women. Yet we do not read of so much as a domestic quarrel in the catalogue. The official view is that this is irrelevant: we should judge the man by his art, not by his life. Yet when the two appear so inextricably, obsessively linked before our eyes, we cannot but wonder what lies beneath the surface. Given that he paints his own flesh and blood with such stark realism, the biographical airbrushing jars.

Ultimately, it becomes irresistible to consider how Mr Freud's famous grandfather might interpret paintings that are so autobiographical and yet so repressed. Would he observe the phallic references in the way Mr Freud depicts paintbrushes and unusually well-endowed men, particularly himself in the striking nude self-portrait? Might he psychoanalyse the oedipal quality of Mr Freud's portrait of his mother with his mistress in the background? And what would he make of the contrast between the youthful-looking 79-year-old, as portrayed in the photograph at the front of the catalogue, and the morass of impasto paint coalescing around the face in the Dorian Gray-like self-portrait that was so new it was still drying on the gallery walls as the exhibition opened. Mr Freud's powerful paintings cry out for

narratives but, in the end, they give almost nothing away.

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“Lucian Freud” continues at Tate Britain until September 22nd. It then goes on to Fundacio La Caixa, Barcelona, from October 22nd-January 12th 2003, and to the Museum of Contemporary Art, Los Angeles, from February 9th-May 25th. Catalogue: Abrams; 240 pages; $49.95. Tate Publishing; £34.99. Lucian Freud curates an exhibition of Constable's painting at the Grand Palais, Paris, from October 10th-January 13th 2003

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# The troubles in Ireland

Jul 4th 2002
From The Economist print edition

Still confused about Sinn Fein and the Unionists? “Endgame in Ireland”, Norma Percy's award-winning film—which goes out on PBS from July 7th and, four days later, on Arte in France and Germany—clarifies 20 years of history. The book of the series, by Eamonn Mallie and David McKittrick, is published by Hodder & Stoughton; 314 pages; £12.99

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The history of socialism

# Some uncommon common people

Jul 4th 2002
From The Economist print edition

IN 1895, Edith Lanchester, a member of the Battersea branch of the Marxist Social Democratic Federation (SDF), in south London, told her upper-middle-class family that she was going to live with a self-educated fellow member and worker, an Irishman named James Sullivan. Her brothers seized her, bound her by the wrists and had her committed to a lunatic asylum—from which commissioners reluctantly released her after a press campaign was stirred up by Sullivan and some fellow members. Lanchester's cause had been taken up with some reluctance both by the SDF and the Independent Labour Party, who were all too aware that many of their members would be more shocked by Lanchester's own actions than by her brothers'.

The story says much about socialism—and not just early socialism. Part of the reason why so many radicals, especially cultural radicals, turned to socialism was to shock the bourgeoisie. The working class took it up as a means of getting rid of the bourgeoisie, or, more often, of getting more out of them. Geoff Eley says rather more about the first than the second; he goes in some detail into the suffragette movement and the struggle to obtain the vote for women, seeing that as a quintessentially socialist movement, albeit one that socialists often had to be forced to recognise for what it was.

Forging Democracy: The History of the Left in Europe, 1850-2000
By Geoff Eley

*Oxford University Press; 720 pages; $74 and £25 (hardback), $35 and £19.99 (paperback)*

Buy it at
Amazon.com
Amazon.co.uk

Histories of socialism can sometimes downgrade and lose sight of the fact that this was a movement in which poor people believed and which they, to a significant degree, built. But Mr Eley tells the story well. One of the book's great virtues is that many of the men and women, especially those of lower-class birth who furthered the cause, are given biographies and space. While perhaps not enough is made of the fact that the 20th century's two great tyrannies sprang out of socialism, some uncommon common people are accorded space, at least.

The book's limits, however, lie in the author being too much of a fan of the movements he describes—especially of leftist versions of democratic socialism. A book on European socialism which professes to end in 2000 and says nothing about Tony Blair (but gives Tony Benn generous space) and nothing about Gerhard Schröder (though Oskar Lafontaine is given a mention) betrays a certain bias. In a limp explanation, Mr Eley says that “the rather inchoate political arrangements glimpsed briefly at the end of the 1990s which returned socialist parties to government need definition”—but he hasn't the time. Actually, these movements were quite choate, and under way for a decade before the end of his period. They have also redefined democratic socialism and thus demand discussion, even if tentative.

The same attitude gives rise to some silly judgments—such as the adoption of an off-the-shelf leftist condemnation of post-communist Eastern Europe's bumpy ride to the market as “disastrous”. On the other hand, much of the history, while lacking the narrative elan of Donald Sassoon's “One Hundred Years of Socialism”, which was equally but less intrusively committed, is straightforward and often insightful.

Intellectuals still find it hard to be clear- sighted about socialism. Mr Eley's eyes mist over in affection for such groups as the Italian Communist Party, and they narrow sharply when his thoughts turn to modern social-democratic parties and their governments, which he regards as “shrivelled in ambition”. He fears that the day when social justice will be struck from the agenda and when capitalism will become impervious to ethical critique is “perilously close”. That in itself is an intellectually shrivelled view, one which sees human emancipation and freedom as only possible under socialism. Social justice, as well as ethics, are both certainly doomed if that is so.

Forging Democracy: The History of the Left in Europe, 1850-2000.
By Geoff Eley.
*Oxford University Press; 720 pages; $74 and £25 (hardback), $35 and £19.99 (paperback)*

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**New American fiction**

# To hell and back

Jul 4th 2002
From The Economist print edition

JONATHAN SAFRAN FOER has created the literary equivalent of a Marc Chagall *shtetl* painting in his exuberant first novel, “Everything is Illuminated”. The novel tells two stories, reversed in order until they collide, as all tales of European 20th-century Jewry inevitably must, in the hideous cataclysm of the Holocaust.

The first story is narrated by the author's bland fictional alter-ego, Jonathan Safran Foer, who travels from America to Ukraine in 1997 in search of the gentile woman in a faded photograph who saved his grandfather from the Nazis. He wants to scratch at “the itch of memory” by visiting what remains of Trachimbrod, his family's ancestral village. But his physical journey into the past triggers a far more vibrant imaginative journey forward from the day in 1791 when his great-great-grandmother emerged Moses-like as a baby from the waters of the River Brod. She founded a fabulous dynasty of dreamers and fornicators, truth-tellers and downright liars; the good, and not so good people of Trachimbrod.

We also have the character of Alex Perchov, a Ukrainian fixer and amateur translator with a flair for spectacular malapropisms. He accompanies the author on his literal and literary journey, offering an epistolary commentary on the chapters that Jonathan sends him from his book in progress, while excavating back into his own family's hidden past. In particular he wants to know why his grandfather cries so much at night. Alex's incompetence in English is a rich source (some might say too rich) of linguistic jokes in the novel, but through the faux-naivety that his unusual vocabulary provides Alex is able to stumble on the truth of both his and Jonathan Safran Foer's family stories. And everything, as he would say, is illuminated.

“Humorous is the only truthful way to tell a sad story,” Alex tells us. The author has energetically raided the traditions and Yiddish vocabulary of Jewish humour to paint a vivid and hectic portrait of the lost world of European Jewry, whose inhabitants squabble and cheat, love and lust their way into oblivion, wilfully blind to the apocalyptic fate that awaits them.

Everything is Illuminated.
By Jonathan Safran Foer.
*Houghton Mifflin; 288 pages; $24.*
*Hamish Hamilton; £14.99*

Everything is Illuminated
By Jonathan Safran Foer

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**Bestsellers in Australia and Canada**

# What the world is reading

Jul 4th 2002
From The Economist print edition

**From stone-age fantasy to carpet wars and contemporary politics**

LIKE the nation itself, Australia's bestseller lists live and breathe diversity. In fiction, there's realism and fantasy, mystery and romance, comedy and high seriousness. Home-grown talent—such as Tim Winton's exceptional tale of love and loss, “Dirt Music”—holds its own alongside foreign heavyweights. The non-fiction list is no less varied, the usual self-help fodder being offset by books on world politics, science, travel and humour (any book called “The Meaning of Life” has, after all, got to be a joke).

A healthy proportion of local writers is a feature of the Canadian lists, too, which includes titles by such novelists and short-story writers as Nino Ricci and Lisa Moore, as well as biographies of two of its native sons, Neil Young and Michael J. Fox. But Canadian readers—like their Australian counterparts—are also eager to learn more about Islam and the Arab world; studies of fundamentalism, Middle-Eastern trade routes and the place of women in Afghan society feature on both lists.

## Bestsellers

| | AUSTRALIAN FICTION | AUSTRALIAN NON-FICTION |
|---|---|---|
| 1 | **Artemis Fowl: The Arctic Incident**<br>*by Eoin Colfer*<br>Follow-up fantasy | **Recollections of a Bleeding Heart**<br>*by Don Watson*<br>Biography of former prime minister Paul Keating |
| 2 | **The Nanny Diaries**<br>*by Emma McLaughlin and Nicola Kraus*<br>Mary Poppins goes to Manhattan | **The Clash of Fundamentalisms**<br>*by Tariq Ali*<br>Survey of Islamic extremism |
| 3 | **The Shelters of Stone**<br>*by Jean M. Auel*<br>Fifth instalment in prehistoric saga | **Can't Lose Weight? You Could Have Syndrome X**<br>*by Sandra Cabot*<br>Chemical imbalance and weight loss |
| 4 | **Moral Hazard**<br>*by Kate Jennings*<br>Working woman in a man's world | **The Tears of Strangers**<br>*by Stan Grant*<br>TV presenter's memoirs |
| 5 | **The Fathomless Caves**<br>*by Kate Forsyth*<br>Prophets, sorcerers and apocalypse | **Almost French**<br>*by Sarah Turnbull*<br>Francophile travel memoir |
| 6 | **Atonement**<br>*by Ian McEwan*<br>Perils of storytelling | **The Map that Changed the World**<br>*by Simon Winchester*<br>Foundations of modern geology |
| 7 | **Dirt Music**<br>*by Tim Winton*<br>Australian love triangle | **7 Days to Strip Fat Forever**<br>*by Shane Bilsborough*<br>Speedy slimming |
| 8 | **Gone for Good**<br>*by Harlan Coben*<br>Search for missing, murderous brother | **The Carpet Wars**<br>*by Christopher Kremmer*<br>Travelling ancient Islamic trade routes |
| 9 | **Sea Glass**<br>*by Anita Shreve*<br>Fortune's Rocks beach revisited | **The Meaning of Life**<br>*by Bradley Trevor Greive*<br>Light-hearted take on an age-old question |
| 10 | **Charlotte Gray**<br>*by Sebastian Faulks*<br>Romantic thriller | **Who Moved My Cheese?**<br>*by Spencer Johnson*<br>Million-selling self-help book |

| | CANADIAN FICTION | CANADIAN NON-FICTION |
|---|---|---|
| 1 | **Family Matters**<br>*by Rohinton Mistry*<br>Ailing patriarch at the mercy of his children | **Stupid White Men**<br>*by Michael Moore*<br>What's wrong with America today |
| 2 | **Unless**<br>*by Carol Shields*<br>Family crisis and linguistic musings | **What Went Wrong?**<br>*by Bernard Lewis*<br>Decline of Islam and the rise of the West |
| 3 | **Crow Lake**<br>*by Mary Lawson*<br>Four children coping with their parents' death | **Self Matters**<br>*by Phillip C. McGraw*<br>Looking after number one |
| 4 | **The Shelters of Stone**<br>*by Jean M. Auel*<br>Fifth instalment in prehistoric saga | **Lucky Man**<br>*by Michael J. Fox*<br>Star's battle with Parkinson's disease |
| 5 | **The Nanny Diaries**<br>*by Emma McLaughlin and Nicola Kraus*<br>Mary Poppins goes to Manhattan | **The Fall of Berlin 1945**<br>*by Antony Beevor*<br>Wartime history |
| 6 | **Testament**<br>*by Nino Ricci*<br>Fictionalised life of Christ | **Lyndon Johnson: Master of the Senate**<br>*by Robert A. Caro*<br>Third volume of presidential biography |
| 7 | **City of Bones**<br>*by Michael Connelly*<br>Latest Harry Bosch thriller | **Blue Gold**<br>*by Maude Barlow and Tony Clarke*<br>Corporate control of water resources |
| 8 | **Clara Callan**<br>*by Richard B. Wright*<br>Sisters correspond during Great Depression | **Shakey**<br>*by Jimmy McDonough*<br>Biography of hoary rocker Neil Young |
| 9 | **Atonement**<br>*by Ian McEwan*<br>Perils of storytelling | **Con Game**<br>*by Michael Harris*<br>Survey of Canada's prisons |
| 10 | **Open**<br>*by Lisa Moore*<br>Short stories with Newfoundland settings | **Veiled Threat**<br>*by Sally Armstrong*<br>The women of Afghanistan |

Sources: Dymocks Booksellers; Canada.com

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# Pierre Werner

Jul 4th 2002
From The Economist print edition

**Pierre Werner, father of the euro, died on June 24th, aged 88**

AP

Get article background

IN THE end Pierre Werner was mildly surprised that Europeans had meekly abandoned their proud currencies, the franc, mark, lira and so on, and accepted the euro. Perhaps, he suggested, they were weary of arguing. He felt a bit weary himself. He had first suggested a common currency for Europe back in 1960, but had to wait for 42 years before it was launched as real notes and coin six months ago.

Mr Werner is generally accepted as the father of the euro. The euro's paternity is probably shared among the pioneers of what eventually became the European Union. A common currency for Europe is hinted at in the Union's founding treaty signed in Rome in 1957. But Mr Werner became its most public advocate; more than that, a zealot. His European colleagues, who tended to be, in public at least, less zealotish, were content that a scheme they adopted in 1971 that eventually led to the euro should be called the Werner Plan. He would get the credit and, if things went wrong, he could also get the blame.

Neither credit nor blame appeared to matter to Mr Werner. What mattered was ending Europe's terrible tribal wars. Economic problems in Germany had led to the second world war, he said. Now economics would be the peacekeeper. In a speech in 1960 he argued for a common currency called the “euror”, a name soon dropped, perhaps because it sounded like “error”. But Mr Werner persisted, and in his 1971 plan proposed that the economies of European states should come under the control of a central authority in perpetuity. Wouldn't national sovereignty be sacrificed? Of course, he said. That was the idea. A federal Europe? A logical development.

The simple logic of the Werner proposals has vexed European political leaders that have nationalistic voters. None of the 12 members of the Union that have adopted the euro appears to favour a federal state, certainly not France or Germany, the master-builders of European unity. Its prospect frightens many people in Britain from even contemplating joining the euro. Best then to belittle the Werner Plan. Much had happened since it was nodded through all that time ago. Pierre Werner was a good man, but with limited authority. Did you know he was prime minister of Luxembourg for 20 years? Yes, Luxembourg, an odd country in some ways.

## How very European

As a fervent European Mr Werner could not have chosen to be born in a more suitable place. Luxembourg was ruled at various times by many other European countries, among them France, Spain, Austria and even the Netherlands. Sometimes the country was sold or given away: its handy size, only 84km (51 miles) by 52km, made it easy to package as a gift to seal an alliance. Germany ignored Luxembourg's pleas of neutrality and occupied it during both world wars.

Mr Werner was brought up bilingually. His father spoke French and his mother German. He set out to be a lawyer and took a law degree in Paris. Then economics took his fancy and at the outbreak of the second world war he was working for a bank in the Luxembourg capital, also called Luxembourg. With memories of the first world war still fresh, many people fled to safer places. Grand Duchess Charlotte, the head of the royal family, moved to Canada. Mr Werner, newly-wedded, stayed put with his bride.

The German occupation turned out to be worse than it had been in the first world war. Many Luxembourgers were conscripted into the German army. Jews were sent to extermination camps. In 1944 Luxembourg was the setting for one of the biggest battles of the second world war when allied forces were nearly surrounded, suffered huge casualties, and came close to defeat in what became known as the battle of the bulge. The experience of war, the ravaged land, the humiliation of the people, the revenge that followed victory when German collaborators were executed; all this shaped Mr Werner's view of how Europe had to be changed for the betterment of its people (including his five children).

He went into politics, and was elected to his country's parliament in 1945. He rose swiftly and served two long stints as prime minister. But Mr Werner outgrew Luxembourg. He became close to Jean Monnet and others who were creating the Common Market, the forebear of the Union. In his memoirs Mr Werner wrote, “To awake Europeans to the weakness and division of Europe became an intellectual obligation for me.”

In those heroic days, no one seemed to question that the central aim of European unity was to prevent war. Economic gain, though useful, was a secondary consideration. Later, Mr Werner noted sadly, economic gain seemed to have become all important for the Union's members and applicants. Luxembourg itself has become immensely rich, partly as a result of being a founder member of the Union. Britain's decision on whether to adopt the euro may turn on five economic tests.

But while Europeans no longer fought each other, many other tribes around the world still did. Mr Werner said there was a road to peace: gradual economic union leading to a single currency for the world. Mondo, he said, would be a suitable name. There may be quite a long wait.

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# Overview

Jul 4th 2002
From The Economist print edition

**Economic optimism** sagged on both sides of the Atlantic. In America, the University of Michigan's consumer-sentiment index fell to 92.4 in June, after growing strongly during the autumn and winter. The euro area's economic-sentiment indicator, a measure of business confidence, fell slightly to 99.6 in June.

**American manufacturers**, in contrast, are cheering up. The ISM's purchasing managers' index rose to 56.2 in June from 55.7 in May.

**Stockmarkets** fell further. America's S&P 500 fell to its lowest since January 1998; Britain's FTSE 100 fell to a five-year low.

Consumer-price inflation in the **euro area** fell to 1.7% in June, a two-year low. This is the first time since May 2000 that it has been below the European Central Bank's 2.0% ceiling.

Revised figures found some growth in the **British** economy: GDP grew at an annual rate of 0.7% in the first quarter, rather than standing still as previously thought.

**Japanese** industrial production fell by 2.2% in the year to May, but grew by 3.9% during the month. Corporate confidence also seems to be rebounding. The quarterly Tankan survey of big manufacturers rose for the second straight quarter to minus 18, up from minus 38 in March, the survey's biggest gain ever. But unemployment rose to 5.4% in May, up from 5.2% in April.

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# Output, demand and jobs

Jul 4th 2002
From The Economist print edition

% change at annual rate

| | GDP | | The Economist poll GDP forecasts | | Industrial production | Retail sales (volume) | Unemployment % rate | |
|---|---|---|---|---|---|---|---|---|
| | 1 qtr | 1 year | 2002 | 2003 | latest | latest | latest | year ago |
| **Australia** | + 3.6 | + 4.2 Q1 | + 4.0 | + 3.9 | + 4.3 Q1 | + 5.0 Q1 | 6.3 May | 6.8 |
| **Austria** | – 0.7 | – 0.4 Q4 | + 1.2 | + 2.6 | + 3.5 Apr | + 0.2 Mar | 4.1 May | 3.5 |
| **Belgium** | + 2.0 | – 0.3 Q1 | + 1.4 | + 3.1 | + 3.8 Apr | + 1.8 Apr | 10.4 May* | 10.0 |
| **Britain** | + 0.7 | + 1.1 Q1 | + 1.7 | + 3.0 | – 4.1 Apr | + 5.4 May | 5.2 Apr† | 5.0 |
| **Canada** | + 6.0 | + 2.1 Q1 | + 3.2 | + 3.6 | + 1.3 Apr | + 5.1 Apr | 7.7 May | 7.0 |
| **Denmark** | + 1.4 | + 1.1 Q1 | + 1.6 | + 2.4 | – 0.8 Apr | + 1.5 Apr | 5.0 Apr | 5.4 |
| **France** | + 1.4 | + 0.3 Q1 | + 1.4 | + 2.9 | + 0.9 Apr | – 0.6 Apr | 9.1 May | 8.6 |
| **Germany** | + 0.7 | – 1.2 Q1 | + 0.9 | + 2.6 | – 2.0 Apr | – 1.9 Apr | 9.7 May‡ | 9.2 |
| **Italy** | + 0.6 | + 0.1 Q1 | + 1.2 | + 2.8 | + 0.5 Apr | – 1.2 Apr | 9.0 Apr | 9.5 |
| **Japan** | + 5.7 | – 1.6 Q1 | – 0.4 | + 1.2 | – 2.2 May | – 2.7 Apr | 5.4 May | 4.9 |
| **Netherlands** | nil | nil Q1 | + 1.2 | + 2.8 | – 5.6 Apr | – 0.2 Mar | 2.3 May§ | 1.9 |
| **Spain** | + 2.1 | + 2.0 Q1 | + 2.2 | + 3.3 | +10.0 Apr | na | 11.4 May** | 10.6 |
| **Sweden** | + 1.1 | + 1.1 Q1 | + 1.7 | + 2.9 | + 0.4 Apr | + 4.7 Apr | 3.4 May* | 3.5 |
| **Switzerland** | + 0.7 | + 0.2 Q1 | + 1.1 | + 2.3 | – 8.8 Q1 | + 4.3 Apr | 2.5 May* | 1.7 |
| **United States** | + 6.1 | + 1.7 Q1 | + 2.8 | + 3.5 | – 1.6 May | + 4.9 May | 5.8 May | 4.4 |
| **Euro area** | + 0.9 | + 0.1 Q1 | + 1.2 | + 2.8 | – 1.2 Apr | + 0.1 Apr | 8.3 May** | 8.0 |
| **MORE COUNTRIES** | Data for the countries below are not provided in printed editions of *The Economist* | | | | | | | |
| **Finland** | – 0.6 | – 2.0 Q1 | na | na | + 0.2 May | + 2.0 Mar | 11.9 May* | 11.3 |
| **Greece** | na | + 4.3 Q1 | na | na | + 4.9 Apr | +19.3 Mar | na | na |
| **Iceland** | na | + 3.12001 | na | na | + 3.3 2001 | na | 2.5 May* | 1.6 |
| **Ireland** | na | nil Q4 | na | na | – 3.3 Apr | – 0.5 Apr | 4.2 May | 3.7 |
| **Luxembourg** | na | + 3.52001 | na | na | – 7.1 Mar | +15.3 Jan | 2.8 Apr | 2.5 |
| **New Zealand** | + 4.3 | + 4.0 Q1 | na | na | + 3.5 Q4 | + 8.2 Q1 | 5.3 Q1 | 5.4 |
| **Norway** | – 1.1 | + 1.0 Q1 | na | na | + 3.9 Apr | + 2.7 May | 4.1 Q1 | 3.7 |
| **Portugal** | + 1.8 | + 1.0 Q4 | na | na | + 1.0 Apr | – 0.2 Apr | 4.4 Q1* | 4.2 |

*Not seasonally adjusted. †Feb-Apr; claimant count rate 3.1% in May. ‡EU harmonised rate 8.1% in Apr. §Mar-May. **Revised series.

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# Prices and wages

Jul 4th 2002
From The Economist print edition

% change at annual rate

| | Consumer prices | | | The Economist poll consumer prices forecast | | Producer prices | | | Wages/earnings | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | latest | | year ago | 2002 | 2003 | latest | | year ago | latest | | year ago |
| **Australia** | + 2.9 | Q1 | + 6.0 | + 2.7 | + 2.6 | + 0.5 | Q1 | + 5.2 | + 4.3 | Q1 | + 5.6 |
| **Austria** | + 1.9 | May | + 3.4 | + 1.8 | + 1.7 | – 0.8 | May | + 3.1 | + 2.4 | May | + 2.7 |
| **Belgium** | + 0.9 | Jun | + 2.9 | + 1.9 | + 1.6 | + 2.4 | May | + 1.7 | + 3.1 | Q1 | + 1.9 |
| **Britain** | + 1.1 | May | + 2.1 | + 2.1 | + 2.5 | + 0.1 | May | + 0.7 | + 3.3 | Apr | + 5.2 |
| **Canada** | + 1.0 | May | + 3.9 | + 1.7 | + 2.2 | – 2.6 | May | + 2.8 | + 2.8 | Apr | + 1.5 |
| **Denmark** | + 2.1 | May | + 2.7 | + 2.3 | + 2.1 | – 0.3 | May | + 2.9 | + 4.0 | Q1 | + 3.8 |
| **France** | + 1.4 | May | + 2.3 | + 1.8 | + 1.5 | – 1.5 | May | + 2.8 | + 3.9 | Q1 | + 4.3 |
| **Germany** | + 0.9 | Jun | + 3.1 | + 1.5 | + 1.4 | – 1.3 | May | + 4.0 | + 2.1 | Apr | + 1.5 |
| **Italy** | + 2.2 | Jun | + 3.0 | + 2.3 | + 2.0 | – 0.9 | May | + 2.9 | + 2.3 | Apr | + 2.6 |
| **Japan** | – 0.9 | May | – 0.7 | – 1.0 | – 0.4 | – 0.9 | May | + 0.9 | – 0.5 | May | – 0.1 |
| **Netherlands** | + 3.3 | May | + 4.9 | + 3.6 | + 2.5 | – 0.7 | Apr | + 6.2 | + 3.2 | May | + 4.9 |
| **Spain** | + 3.6 | May | + 4.2 | + 3.3 | + 2.8 | + 0.6 | May | + 2.7 | + 4.0 | Q1 | + 3.4 |
| **Sweden** | + 2.0 | May | + 3.0 | + 2.4 | + 2.1 | – 0.2 | May | + 2.6 | + 2.0 | Apr | + 3.1 |
| **Switzerland** | + 0.3 | Jun | + 1.6 | + 0.8 | + 1.2 | – 1.4 | May | + 0.4 | + 2.5 | 2001 | + 1.3 |
| **United States** | + 1.2 | May | + 3.6 | + 1.7 | + 2.3 | – 2.7 | May | + 3.9 | + 3.2 | May | + 4.2 |
| **Euro area** | + 1.7 | Jun | + 3.0 | + 2.2 | + 1.8 | – 0.9 | May | + 3.7 | + 3.1 | Q4 | + 2.5 |
| **MORE COUNTRIES** | Data for the countries below are not provided in printed editions of *The Economist* | | | | | | | | | | |
| **Finland** | + 1.3 | May | + 3.3 | na | na | – 1.6 | May | + 2.1 | + 3.2 | Q1 | + 5.1 |
| **Greece** | + 3.4 | May | + 3.6 | na | na | + 3.1 | Apr | + 5.1 | na | | na |
| **Iceland** | + 4.8 | Jun | + 6.8 | na | na | + 7.1 | Jun | + 5.9 | + 7.5 | May | + 8.0 |
| **Ireland** | + 4.7 | May | + 5.4 | na | na | + 0.3 | May | + 3.4 | + 8.9 | Q1 | + 7.4 |
| **Luxembourg** | + 1.9 | May | + 3.3 | na | na | – 2.5 | Apr | + 2.6 | + 0.1 | Mar | + 6.7 |
| **New Zealand** | + 2.6 | Q1 | + 3.1 | na | na | + 2.8 | Q1 | + 8.0 | + 2.1 | Q1 | + 1.8 |
| **Norway** | + 0.4 | May | + 4.3 | na | na | –11.3 | May | + 4.6 | + 4.6 | Q1 | + 4.4 |
| **Portugal** | + 3.3 | May | + 4.8 | na | na | – 2.0 | May | + 5.5 | na | | na |

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# Economic forecasts

Jul 4th 2002
From The Economist print edition

**The Economist poll of forecasters, July averages** (previous month's, if changed)

| | Real GDP, % change Low/high range | | Real GDP, % change average | | Consumer prices % increase | | Current account % of GDP | |
|---|---|---|---|---|---|---|---|---|
| | 2002 | 2003 | 2002 | 2003 | 2002 | 2003 | 2002 | 2003 |
| **Australia** | 2.8/4.5 | 3.4/4.5 | 4.0 | 3.9 | 2.7 (2.6) | 2.6 (2.5) | -3.3(-3.5) | -3.6 |
| **Austria** | 0.5/1.7 | 2.1/3.4 | 1.2 (1.3) | 2.6 (2.7) | 1.8 (1.7) | 1.7 | -2.2 | -2.0 |
| **Belgium** | 0.5/2.6 | 2.4/3.9 | 1.4 | 3.1 | 1.9 (2.0) | 1.6 (1.7) | 5.0 (5.1) | 5.3 |
| **Britain** | 1.2/2.2 | 2.4/3.5 | 1.7 (1.8) | 3.0 | 2.1 | 2.5 | -2.2 | -2.1 |
| **Canada** | 2.1/3.7 | 3.0/4.7 | 3.2 (2.9) | 3.6 | 1.7 (1.5) | 2.2 (2.1) | 2.2 | 2.3 (2.5) |
| **Denmark** | 1.3/1.9 | 2.0/2.9 | 1.6 | 2.4 (2.5) | 2.3 (2.4) | 2.1 | 1.9 | 1.9 |
| **France** | 1.2/1.8 | 2.4/3.5 | 1.4 | 2.9 | 1.8 | 1.5 | 1.8 (1.7) | 1.7 |
| **Germany** | 0.6/1.2 | 1.8/3.7 | 0.9 | 2.6 (2.7) | 1.5 (1.6) | 1.4 | 1.1 (0.7) | 1.1 (0.8) |
| **Italy** | 0.6/1.7 | 2.0/3.3 | 1.2 (1.3) | 2.8 (2.9) | 2.3 (2.2) | 2.0 (2.1) | 0.1 | nil |
| **Japan** | -1.0/1.1 | 0.3/2.1 | -0.3 (-0.8) | 1.2 | -1.0 (-0.9) | -0.4 (-0.6) | 2.7 (2.6) | 2.7 (2.6) |
| **Netherlands** | 0.5/1.6 | 2.0/3.4 | 1.2 (1.4) | 2.8 (2.9) | 3.6 | 2.5 | 4.0 (3.7) | 4.1 (4.0) |
| **Spain** | 2.0/2.5 | 2.5/4.0 | 2.2 | 3.3 | 3.3 (3.1) | 2.8 (2.6) | -2.2(-2.1) | -1.9 (-1.8) |
| **Sweden** | 1.4/2.1 | 2.5/3.2 | 1.7 (1.8) | 2.9 (3.0) | 2.4 | 2.1 | 3.2 (3.1) | 3.3 (3.2) |
| **Switzerland** | 0.6/1.9 | 1.6/2.9 | 1.1 | 2.3 | 0.8 | 1.2 | 9.8 (9.7) | 10.1 (9.9) |
| **United States** | 2.4/3.1 | 2.8/4.2 | 2.8 (2.9) | 3.5 | 1.7 (1.6) | 2.3 | -4.3(-4.2) | -4.6 (-4.5) |
| **Euro area** | 0.9/1.8 | 2.2/3.7 | 1.2 (1.3) | 2.8 (2.9) | 2.2 (2.1) | 1.8 | 0.4 (0.3) | 0.5 (0.4) |

Sources: ABN Amro, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, Merrill Lynch, J.P. Morgan Chase, Morgan Stanley, Nordbanken, Decision Economics, BNP Paribas, Royal Bank of Canada, Schroder Salomon Smith Barney, Scotiabank, Shinsei Bank, UBS Warburg

Each month *The Economist* surveys a group of forecasters and calculates the average of their predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table also shows the highest and lowest projections for growth. The previous month's forecasts, where different, are shown in brackets. This month the panel has become slightly more pessimistic about the outlook for America and for the euro zone, but has revised up its forecasts for Japan. It now expects America's economy to grow by 2.8% in 2002, down from 2.9% last month. Growth in the euro area, the panel estimates, will be less than half as strong, at 1.2%. Inflation forecasts for 2002 have been revised up to 1.7% for America, and to 2.2% for the euro area. Japanese deflation is expected to continue, and the economy may shrink by 0.3% in 2002, better than last month's forecast of a 0.8% fall.

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# Money and interest rates

Jul 4th 2002
From The Economist print edition

| | Money supply* % change on year ago | | | Interest rates % p.a. (Jul 3rd 2002) | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | | | 3-mth money market | | 2-year | 10-year gov't bonds | | corporate |
| | narrow | broad | | latest | year ago | gov't bonds | latest | year ago | bonds |
| **Australia** | + 3.7 | +14.9 | May | 5.00 | 5.05 | 5.34 | 6.02 | 6.20 | 7.10‡ |
| **Britain** | + 9.0 | + 6.0 | May | 4.09 | 5.25 | 4.61 | 5.01 | 5.28 | 6.05 |
| **Canada** | +13.6 | + 5.5 | May | 2.75 | 4.34 | 3.79 | 5.39 | 5.92 | 6.87 |
| **Denmark** | + 7.4 | + 8.3 | May | 3.68 | 4.85 | 4.40 | 5.13 | 5.33 | 6.94 |
| **Japan** | +31.9 | + 3.5 | May | 0.03 | 0.01 | 0.06 | 1.31 | 1.25 | 1.39 |
| **Sweden** | + 2.5 | + 7.3 | Apr | 4.29 | 4.28 | 4.84 | 5.37 | 5.45 | 5.41 |
| **Switzerland** | + 4.1 | + 3.0 | May | 1.20 | 3.25 | 1.85 | 3.08 | 3.38 | 4.19 |
| **United States** | + 5.9 | + 7.8 | May | 1.74 | 3.69 | 2.76 | 4.74 | 5.38 | 6.73 |
| **Euro area**† | + 7.0 | + 7.8 | May | 3.43 | 4.45 | 3.87 | 4.87 | 5.05 | 5.98 |

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. ‡ New series. Benchmarks: US 30-year 5.43%, Japan No.240 1.32%. Central bank rates: US fed funds 1.75%, ECB refinancing 3.25%, BOJ overnight call 0.001%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS Warburg, DRI-WEFA, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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# The Economist commodity price index

Jul 4th 2002
From The Economist print edition

1995=100

| | Jun 25th | Jul 2nd* | % change on one month | % change on one year |
|---|---|---|---|---|
| **Dollar index** | | | | |
| All items | 70.6 | 72.6 | + 3.8 | + 5.7 |
| Food | 70.6 | 73.5 | + 4.4 | + 8.2 |
| Industrials | | | | |
| All | 70.5 | 71.4 | + 3.1 | + 2.5 |
| Nfa† | 73.2 | 72.8 | + 4.9 | + 6.8 |
| Metals | 68.3 | 70.1 | + 1.6 | - 1.0 |
| **Sterling index** | | | | |
| All items | 74.2 | 74.8 | - 0.8 | - 2.8 |
| **Euro index** | | | | |
| All items | 95.7 | 96.8 | - 0.6 | - 9.2 |
| **Yen index** | | | | |
| All items | 91.5 | 92.8 | + 0.7 | + 2.0 |
| **Gold** | | | | |
| $ per oz | 318.35 | 314.25 | - 3.4 | +17.1 |
| **West Texas Intermediate** | | | | |
| $ per barrel | 26.30 | 26.86 | + 8.0 | + 2.1 |

* Provisional. † Non-food agriculturals.

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# Stockmarkets

Jul 4th 2002
From The Economist print edition

Market indices

| | Jul 3rd | 2002 high | 2002 low | % change on one week | % change on record high | % change on Dec 31st 2001 in local currency | % change on Dec 31st 2001 in $ terms |
|---|---|---|---|---|---|---|---|
| Australia (All Ordinaries) | 3,132.9 | 3,440.0 | 3,129.7 | + 0.1 | - 8.9 | - 6.8 | + 1.8 |
| Austria (ATX) | 1,222.3 | 1,357.2 | 1,114.4 | - 0.8 | -29.6 | + 7.2 | +18.0 |
| Belgium (Bel 20) | 2,408.5 | 2,899.8 | 2,402.2 | - 1.4 | -34.6 | -13.4 | - 4.7 |
| Britain (FTSE 100) | 4,392.6 | 5,323.8 | 4,392.6 | - 3.1 | -36.6 | -15.8 | -11.7 |
| Canada (Toronto Composite) | 7,024.1 | 7,958.1 | 7,013.4 | nil | -38.3 | - 8.6 | - 4.9 |
| Denmark (KBX) | 201.1 | 233.4 | 196.3 | + 1.3 | -33.3 | -10.5 | - 1.4 |
| France (SBF 250) | 2,425.1 | 3,081.9 | 2,425.1 | - 2.0 | -44.8 | -18.7 | -10.4 |
| (CAC 40) | 3,623.3 | 4,688.0 | 3,623.3 | - 2.1 | -47.7 | -21.7 | -13.7 |
| Germany (Xetra DAX) | 4,138.2 | 5,462.6 | 4,099.1 | + 1.0 | -48.7 | -19.8 | -11.7 |
| Italy (BCI) | 1,234.9 | 1,513.0 | 1,219.0 | + 1.3 | -43.4 | -13.8 | - 5.1 |
| Japan (Nikkei 225) | 10,812.3 | 11,979.9 | 9,420.9 | + 7.3 | -72.2 | + 2.6 | +12.2 |
| (Topix) | 1,044.2 | 1,139.4 | 922.5 | + 6.1 | -63.8 | + 1.2 | +10.6 |
| Netherlands (AEX) | 406.1 | 531.2 | 406.1 | - 1.7 | -42.1 | -19.9 | -11.8 |
| Spain (Madrid SE) | 696.2 | 848.1 | 696.2 | - 0.7 | -39.3 | -15.6 | - 7.0 |
| Sweden (Affarsvarlden Gen) | 170.1 | 236.8 | 166.1 | - 0.5 | -57.5 | -26.5 | -17.0 |
| Switzerland (Swiss Market) | 5,711.4 | 6,694.1 | 5,594.2 | + 1.5 | -32.1 | -11.0 | - 1.0 |
| United States (DJIA) | 9,055.0 | 10,635.3 | 9,007.8 | - 0.7 | -22.8 | - 9.6 | - 9.6 |
| (S&P 500) | 954.0 | 1,172.5 | 948.1 | - 2.0 | -37.5 | -16.9 | -16.9 |
| (Nasdaq Comp) | 1,380.2 | 2,059.4 | 1,357.9 | - 3.4 | -72.7 | -29.2 | -29.2 |
| Europe (FTSE Eurotop 300)* | 1,013.8 | 1,279.7 | 1,013.8 | - 1.2 | -40.5 | -19.6 | -11.5 |
| Euro area (FTSE Ebloc 100)* | 869.4 | 1,125.1 | 869.4 | - 1.1 | -43.9 | -21.8 | -13.9 |
| World (MSCI)† | 873.2 | 1,024.4 | 873.2 | - 1.3 | -39.7 | na | -13.0 |
| World bond market (Salomon)‡ | 482.2 | 485.6 | 430.3 | - 0.7 | + 4.8 | na | + 9.7 |

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms. ‡Salomon Smith Barney World Government Bond Index, total return, in $ terms.

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# Trade, exchange rates and budgets

Jul 4th 2002
From The Economist print edition

| | Trade balance*, $bn latest 12 months | | Current account $bn latest 12 mths | | Current account % of GDP, forecast 2002 | Current account % of GDP, forecast 2003 | Exchange rate trade-weighted† Jul 3rd | Exchange rate trade-weighted† year ago | Currency units per $ Jul 3rd | Currency units per $ year ago | Currency units per £ | Currency units per euro | Currency units per ¥100 | Budget balance % of GDP 2002‡ |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Australia | + 0.4 | May | − 9.5 | Q1 | − 3.3 | − 3.6 | 74.5 | 74.1 | 1.79 | 1.93 | 2.73 | 1.76 | 1.49 | 0.1 |
| Austria | − 2.6 | Mar | − 2.5 | Apr | − 2.2 | − 2.0 | 100.8 | 99.6 | 1.02 | 1.18 | 1.56 | – | 0.85 | -0.3 |
| Belgium | + 12.2 | Apr | + 13.0 | Dec | + 5.0 | + 5.3 | 100.2 | 98.0 | 1.02 | 1.18 | 1.56 | – | 0.85 | nil |
| Britain | − 47.1 | Apr | − 31.2 | Q1 | − 2.2 | − 2.1 | 104.3 | 107.9 | 0.66 | 0.71 | – | 0.64 | 0.55 | -0.8 |
| Canada | + 35.6 | Apr | + 14.7 | Q1 | + 2.2 | + 2.3 | 77.5 | 80.0 | 1.53 | 1.51 | 2.34 | 1.50 | 1.28 | 1.0 |
| Denmark | + 7.0 | Apr | + 3.5 | Apr | + 1.9 | + 1.9 | 103.0 | 101.1 | 7.58 | 8.80 | 11.6 | 7.43 | 6.32 | 2.2 |
| France | + 7.1 | Apr | + 24.9 | Apr | + 1.8 | + 1.7 | 103.0 | 100.5 | 1.02 | 1.18 | 1.56 | – | 0.85 | -2.0 |
| Germany | + 94.5 | Apr | + 14.9 | Apr | + 1.1 | + 1.1 | 100.1 | 97.3 | 1.02 | 1.18 | 1.56 | – | 0.85 | -2.8 |
| Italy | + 8.3 | Apr | − 0.3 | Mar | + 0.1 | nil | 73.5 | 71.7 | 1.02 | 1.18 | 1.56 | – | 0.85 | -1.4 |
| Japan | + 73.5 | Apr | + 97.4 | Apr | + 2.7 | + 2.7 | 135.2 | 138.2 | 120 | 124 | 183 | 118 | – | -8.0 |
| Netherlands | + 22.8 | Apr | + 13.6 | Q1 | + 4.0 | + 4.1 | 99.2 | 96.7 | 1.02 | 1.18 | 1.56 | – | 0.85 | 0.1 |
| Spain | − 37.1 | Mar | − 15.3 | Mar | − 2.2 | − 1.9 | 75.1 | 73.5 | 1.02 | 1.18 | 1.56 | – | 0.85 | -0.3 |
| Sweden | + 14.6 | May | + 7.6 | Apr | + 3.2 | + 3.3 | 77.8 | 74.8 | 9.3 | 10.9 | 14.2 | 9.10 | 7.75 | 2.1 |
| Switzerland | + 2.3 | May | + 25.7 | Q1 | + 9.8 | +10.1 | 114.5 | 107.2 | 1.49 | 1.80 | 2.28 | 1.46 | 1.25 | na |
| United States | −423.2 | Apr | −398.1 | Q1 | − 4.3 | − 4.6 | 113.2 | 121.2 | – | – | 1.53 | 0.98 | 0.83 | -1.0 |
| Euro area | + 65.5 | Apr | + 16.0 | Apr | + 0.4 | + 0.5 | 81.8 | 76.2 | 1.02 | 1.18 | 1.56 | – | 0.85 | -1.5 |
| MORE COUNTRIES | Data for the countries below are not provided in printed editions of *The Economist* | | | | | | | | | | | | | |
| Finland | + 12.1 | Apr | + 7.4 | Apr | na | na | 79.0 | 77.2 | 1.02 | 1.18 | 1.56 | – | 0.85 | 3.2 |
| Greece | − 19.1 | Dec | − 7.2 | Dec | na | na | 58.0 | 56.9 | 1.02 | 1.18 | 1.56 | – | 0.85 | 0.4 |
| Iceland | + 0.1 | May | − 0.2 | Q1 | na | na | na | na | 86.4 | 104 | 132 | 84.7 | 72.1 | -0.5 |
| Ireland | + 33.2 | Apr | − 1.1 | Q4 | na | na | 89.6 | 85.5 | 1.02 | 1.18 | 1.56 | – | 0.85 | 0.1 |
| Luxembourg | − 2.9 | Feb | + 0.9 | Q4 | na | na | 100.2 | 98.0 | 1.02 | 1.18 | 1.56 | – | 0.85 | 2.2 |
| New Zealand | + 0.2 | May | − 1.2 | Q1 | na | na | 88.8 | 78.7 | 2.05 | 2.46 | 3.13 | 2.01 | 1.71 | 0.1 |
| Norway | + 25.1 | May | + 25.9 | Apr | na | na | 105.8 | 95.4 | 7.48 | 9.37 | 11.4 | 7.34 | 6.24 | 14.0 |
| Portugal | − 13.1 | Mar | − 9.8 | Mar | na | na | 90.1 | 88.6 | 1.02 | 1.18 | 1.56 | – | 0.85 | -2.4 |

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD forecast.

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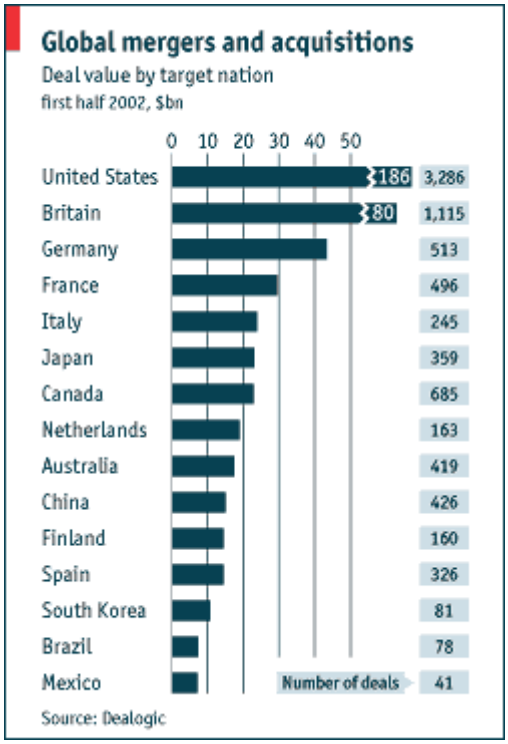
# Global mergers and acquisitions

Jul 4th 2002
From The Economist print edition

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# Overview

Jul 4th 2002
From The Economist print edition

**Turkey's** economy is doing better than expected. GDP grew by 2.3% in the year to the first quarter, after falling by 10.4% in the year to the previous quarter. In the year to June, consumer prices rose by 42.6%, down slightly from the year to May.

Industrial production in **South Korea** climbed by 7.7% in the year to May. Consumer prices fell by 0.1% in June, but rose by 2.6% year-on-year.

**Colombia's** industrial output climbed by 7.8% in the year to April, its best showing so far this year.

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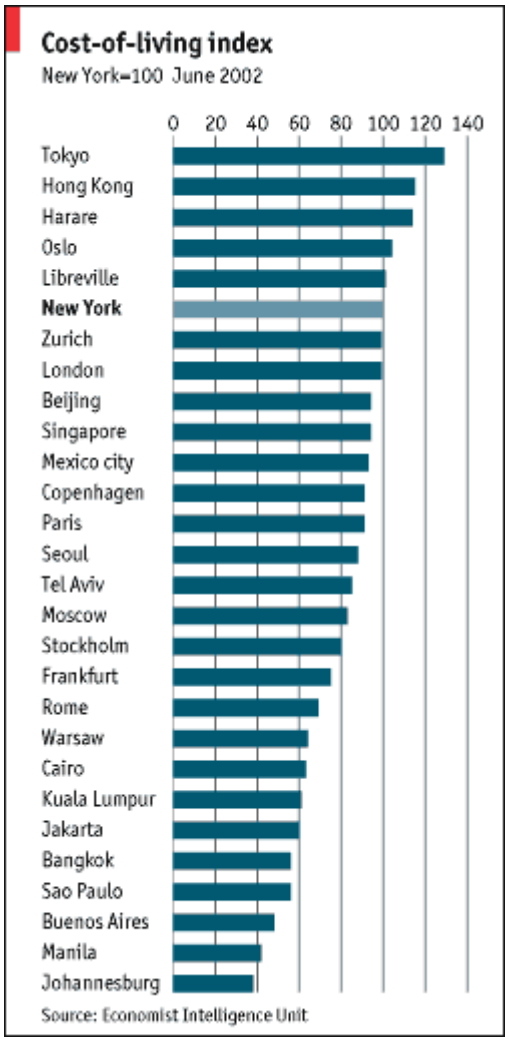
# Cost-of-living index

Jul 4th 2002
From The Economist print edition

The world's most expensive city is Tokyo, according to the latest cost-of-living index prepared by the Economist Intelligence Unit, a sister company of *The Economist*. The index tracks prices in 131 cities compared with New York, which is set at 100. Tokyo is rated at 129, and another Japanese metropolis, Osaka-Kobe, at 127. But not all expensive cities are in rich countries or booming economies. Largely because of Zimbabwe's overvalued currency, Harare is, at 114, more expensive than either New York or London. Johannesburg, in contrast, stands at only 38.

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# Economy

Jul 4th 2002
From The Economist print edition

| | % change on year earlier | | | | | | Latest 12 months, $bn | | | | Foreign reserves* $bn, latest | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | GDP | | Industrial production | | Consumer prices | | Trade balance | | Current account | | | |
| China | + 7.6 | Q1 | +12.9 | May | – 1.1 | May | +25.8 | May | +21.2 | 2001§ | 230.9 | Mar |
| Hong Kong | – 0.9 | Q1 | – 9.3 | Q4 | – 3.1 | May | – 8.8 | May | +12.0 | Q4 | 111.3 | May |
| India | + 6.3 | Q4 | + 2.9 | Apr | + 4.7 | May | – 5.8 | Apr | – 0.1 | Q4 | 52.9 | May |
| Indonesia | + 2.5 | Q1 | – 2.2 | Q3 | +11.5 | Jun | +26.9 | May | + 8.4 | Q3 | 27.9 | May |
| Malaysia | + 1.1 | Q1 | + 3.8 | Apr | + 1.6 | May | +13.2 | May | + 7.0 | Q1 | 32.6 | May |
| Philippines | + 3.8 | Q1 | – 1.2 | Mar | + 3.6 | May | + 2.3 | Apr | + 5.2 | Mar | 14.4 | May |
| Singapore | – 1.7 | Q1 | +17.0 | May | – 0.3 | May | + 6.1 | May | +18.4 | Q1 | 78.2 | May |
| South Korea | + 5.7 | Q1 | + 7.7 | May | + 2.6 | Jun | + 8.9 | May | + 5.9 | May | 109.6 | May |
| Taiwan | + 0.9 | Q1 | +10.1 | May | – 0.3 | May | +18.7 | May | +22.0 | Q1 | 139.8 | May |
| Thailand | + 3.9 | Q1 | + 8.4 | May | + 0.2 | Jun | + 4.2 | May | + 6.5 | May | 34.5 | May |
| Argentina | –16.3 | Q1 | –14.3 | May | +23.0 | May | +11.8 | May | nil | Q1 | 10.2 | May |
| Brazil | – 0.7 | Q1 | + 6.0 | Apr | + 7.8 | May | + 5.3 | Jun | –19.0 | May | 33.0 | Apr |
| Chile | + 1.5 | Q1 | – 3.8 | May | + 2.1 | May | + 2.2 | May | – 1.0 | Q1 | 15.0 | May |
| Colombia | + 0.5 | Q1 | + 7.8 | Apr | + 5.8 | May | + 0.6 | Mar | – 1.7 | Q4 | 10.5 | May |
| Mexico | – 2.0 | Q1 | + 8.0 | Apr | + 4.7 | May | – 9.2 | May | –16.8 | Q1 | 45.1 | Apr |
| Peru | + 7.5 | Apr | – 2.4 | Mar | – 0.2 | Jun | – 0.1 | Apr | – 1.0 | Q1 | 8.7 | May |
| Venezuela | – 4.2 | Q1 | –20.0 | Mar | +18.3 | May | + 8.0 | Q1 | + 1.8 | Q1 | 6.7 | Apr |
| Egypt | + 4.9 | 2001† | + 7.8 | 2001† | + 2.5 | Mar | – 8.6 | Jan | – 0.1 | Q4 | 12.6 | Mar |
| Israel | – 4.2 | Q1 | – 3.5 | Apr | + 5.5 | May | – 5.8 | May | – 2.3 | Q1 | 24.3 | May |
| South Africa | + 2.1 | Q1 | +12.5 | Apr | + 8.4 | May | + 3.8 | May | – 0.1 | Q1 | 5.9 | May |
| Turkey | + 2.3 | Q1 | +14.1 | Apr | +42.6 | Jun | – 8.9 | Apr | + 2.6 | Apr | 22.0 | May |
| Czech Republic | + 2.5 | Q1 | + 8.2 | Apr | + 2.5 | May | – 2.5 | May | – 2.4 | Q1 | 20.2 | May |
| Hungary | + 2.9 | Q1 | – 0.3 | Apr | + 5.6 | May | – 2.3 | Apr | – 1.6 | Apr | 9.8 | May |
| Poland | + 0.5 | Q1 | – 4.1 | May | + 1.9 | May | –10.8 | May | – 7.1 | May | 26.4 | May |
| Russia | + 3.7 | Q1 | + 2.8 | May | +16.2 | May | +44.8 | Apr | +31.2 | Q1 | 38.5 | May |
| **MORE COUNTRIES** | Data for the countries below are not provided in printed editions of *The Economist* | | | | | | | | | | | |
| Pakistan | + 3.3 | 2001† | –10.1 | Feb | + 2.9 | May | – 1.1 | May | + 0.3 | 2001† | 4.1 | May |
| Saudi Arabia | + 1.2 | 2001 | na | | nil | Mar | +44.1 | 2001 | +14.5 | 2001 | 17.7 | Apr |

*Excluding gold, except Singapore; IMF definition. †Year ending June. §Economist Intelligence Unit estimate.

**Text refers only to the first 25 countries listed**

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; Economist Intelligence Unit; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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# Financial markets

Jul 4th 2002
From The Economist print edition

| | Currency units | | | Interest rates | Stockmarkets | % change on | | |
|---|---|---|---|---|---|---|---|---|
| | per $ | | per £ | short-term | Jul 3rd | | Dec 31st 2001 | |
| | Jul 3rd | year ago | Jul 3rd | % p.a. | | one week | in local currency | in $ terms |
| China | 8.28 | 8.28 | 12.6 | na | 1,806.6 | +1.0 | + 5.5 | + 5.5 |
| Hong Kong | 7.80 | 7.80 | 11.9 | 1.83 | 10,579.2 | +2.2 | – 7.2 | – 7.2 |
| India | 48.8 | 47.1 | 74.4 | 6.13 | 3,310.2 | +4.1 | + 1.5 | + 0.3 |
| Indonesia | 8,965 | 11,365 | 13,682 | 15.98 | 478.5 | –5.0 | + 22.1 | + 41.6 |
| Malaysia | 3.80 | 3.80 | 5.80 | 3.25 | 739.4 | +4.9 | + 6.2 | + 6.2 |
| Philippines | 50.7 | 53.0 | 77.4 | 7.63 | 1,141.6 | –2.0 | – 2.3 | – 0.6 |
| Singapore | 1.77 | 1.82 | 2.70 | 0.81 | 1,583.1 | +3.3 | – 2.5 | + 1.8 |
| South Korea | 1,198 | 1,296 | 1,828 | 4.91 | 753.4 | +7.3 | + 8.6 | + 19.1 |
| Taiwan | 33.5 | 34.4 | 51.1 | 2.10 | 5,047.8 | –1.5 | – 9.1 | – 4.9 |
| Thailand | 41.6 | 45.5 | 63.5 | 2.13 | 395.2 | +3.7 | + 30.0 | + 38.3 |
| Argentina | 3.56 | 1.00 | 5.43 | 46.60 | 371.5 | +11.0 | + 25.8 | – 64.6 |
| Brazil | 2.87 | 2.39 | 4.38 | 18.41 | 10,635.5 | –0.5 | – 21.7 | – 36.9 |
| Chile | 698 | 640 | 1,065 | 3.84 | 4,921.0 | –1.5 | – 8.8 | – 13.6 |
| Colombia | 2,428 | 2,304 | 3,706 | 8.21 | 1,224.9 | –1.7 | + 14.4 | + 7.3 |
| Mexico | 9.97 | 9.07 | 15.2 | 8.20 | 6,326.5 | +2.5 | – 0.7 | – 8.7 |
| Peru | 3.52 | 3.52 | 5.38 | 2.67 | 1,109.9 | –2.9 | – 5.6 | – 7.7 |
| Venezuela | 1,281 | 719 | 1,954 | 27.00 | 7,238.3 | –2.3 | + 10.2 | – 34.8 |
| Egypt | 4.64 | 3.93 | 7.09 | 7.20 | 5,314.3 | +1.3 | + 0.8 | – 0.7 |
| Israel | 4.77 | 4.18 | 7.28 | 6.45 | 346.7 | +0.8 | – 22.4 | – 28.2 |
| South Africa | 10.2 | 8.08 | 15.5 | 12.65 | 10,327.0 | –1.3 | – 1.1 | + 16.6 |
| Turkey | 1,620,000 | 1,276,000 | 2,472,444 | 44.00 | 9,008.4 | +4.4 | – 34.6 | – 41.3 |
| Czech Republic | 30.0 | 39.9 | 45.8 | 3.54 | 400.0 | –3.6 | + 1.4 | + 20.2 |
| Hungary | 250 | 285 | 382 | 9.25 | 7,452.9 | +2.9 | + 4.5 | + 14.8 |
| Poland | 4.09 | 4.00 | 6.24 | 9.13 | 13,902.6 | –3.1 | – 0.1 | – 3.5 |
| Russia | 31.5 | 29.2 | 48.1 | 23.00 | 359.3‡ | +7.0 | + 42.8 | + 38.1 |
| EMF (MSCI)* | 1.00 | 1.00 | 1.53 | na | 316.6 | +2.3 | na | – 0.3 |
| EMBI+† | 1.00 | 1.00 | 1.53 | na | 198.3 | +0.5 | na | – 1.0 |

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms.
Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; Economist Intelligence Unit; Reuters; Warburg Dillon Read; JP Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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